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John Kerry chose the right running mate; but it will not solve the problems with his candidacy ... More on this week's lead article

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Politics this week

Jul 8th 2004
From The Economist print edition

A dream team?

AP

John Kerry picked **John Edwards**, a first-term senator from North Carolina, as his vice-presidential running mate. Meanwhile, Mr Kerry collected $34m in campaign funds during June, bringing his total to around $180m.

See article

Construction began at the site of the World Trade Centre on the **Freedom Tower**, a skyscraper that will measure 1,776 feet (541 metres).

The **Roman Catholic** archdiocese in Portland, Oregon, sought bankruptcy protection to ward off some $160m of child-sex lawsuits.

The Defence Department set up a tribunal for 595 detainees at **Guantánamo Bay** to contest their status as “enemy combatants”. They will also be told that they have the right to file *habeas corpus* writs in the United States.

Arnold Schwarzenegger criticised **California's** legislature for failing, as always, to pass the state budget by the end of its fiscal year. Negotiations broke down over funding for local government.

Insurgency measures

Iraq's interim government offered an amnesty to some insurgents, while announcing tough emergency measures, including laws enabling it to impose curfews, make searches and detain suspects in some areas for up to 60 days. Iyad Allawi, the prime minister, also said the death penalty may come back. The insurgency showed no immediate sign of abating.

See article

Mohamed ElBaradei, head of the International Atomic Energy Agency, the UN's nuclear watchdog, visited **Israel**, which is thought to have nuclear weapons though it doesn't acknowledge them. He suggested that the Middle East should become a nuclear-free zone.

See article

The International Court of Justice at The Hague was due on July 9th to rule on whether the Israeli security barrier that cuts through the occupied **West Bank** is illegal. The Israelis say they will ignore the verdict if it goes against them.

See article

A court in **Yemen** charged six Yemenis with planning the attack on an American destroyer, *USS Cole*, in October 2000. The attack, ascribed to al-Qaeda, killed 17 sailors.

The **African Union** offered mild criticism of the human-rights records of Zimbabwe and Sudan. It also promised to send a small armed force to observe events in the western Sudanese region of Darfur, where a state-sponsored campaign of ethnic cleansing threatens to cause famine.

Sudan's government charged 36 members of a Muslim fundamentalist opposition party, led by Hassan al-Turabi, with involvement in a coup attempt said to have been uncovered in March.

Police in **Kenya** shot dead two people and injured several more during protests at the government's failure to honour a promise to revise the constitution to limit the powers of the president.

See article

A poor choice

After the ousting of his finance minister, Giulio Tremonti, **Italy's** prime minister, Silvio Berlusconi, chose to take the job himself. Two days later Standard & Poor's, a credit-rating agency, downgraded Italy's debt, the first time this has happened to a country that is in the euro area.

See article

The opening of the defence case by Slobodan Milosevic at the **war-crimes tribunal in The Hague** was postponed due to the former Yugoslav president's ill health. The Americans pressed the Serbian government to try harder to capture Ratko Mladic, the general allegedly responsible for the Srebrenica massacre in 1995, and send him to The Hague as well.

See article

The parliament of **north Cyprus** voted to hold new elections, probably in September. Northern Turkish-Cypriots voted to endorse a UN reunification plan in April, but southern Greek-Cypriots rejected it. The European Commission proposed to respond to this by giving more help, including money, to the north.

The European Commission is proposing to scrap **Britain's** EU budget rebate and replace it with a general rebate for all big contributors. Britain will fight hard for its money.

See article

Austria's president, Thomas Klestil, died suddenly after suffering heart failure, on the eve of his departure to make way for Heinz Fischer.

The **Greeks** celebrated a highly unlikely triumph by their team in the Euro 2004 football championship. The prime minister declared that the success boded well for the Olympic Games, which begin in just over a month's time.

See article

In the run-off

AFP

Susilo Bambang Yudhoyono came first in an election for **Indonesia's** presidency. But he failed to win 50% of the vote, making a run-off in September necessary.

See article

Nepal's new prime minister, Sher Bahadur Deuba, claimed to have formed a broad-based coalition government aimed at ending political deadlock that has lasted since the king sacked him two years ago.

Bird flu reappeared in Asia, affecting poultry in Thailand, China and Vietnam.

EPA

The head of **China's** space agency said his country plans to send an unmanned mission to the moon in 2007.

Fox in a hole

This was a bad week for **Mexico's** president, Vicente Fox. His conservative National Action Party fared poorly in three state elections. And his chief of staff resigned suddenly, criticising the presidential ambitions of Mr Fox's wife.

See article

The president of **Venezuela's** electoral authority said that a recall referendum next month on President Hugo Chávez could be observed by the Organisation of American States and the Atlanta-based Carter Centre—but only under tight restrictions which both organisations may not find acceptable.

See article

During a visit to London, Leonel Fernández, the president-elect of the **Dominican Republic**, revealed that he would seek a “friendly, market” restructuring of the country's bonds when he takes office next month. The republic's once-flourishing economy has been badly hit by a bank collapse.

More disarray in **Mercosur**, South America's putative common market. On the eve of a summit of the group's presidents, Argentina imposed tariffs of 21% on the import of televisions from Brazil; it also imposed licences for the import of Brazilian white goods.

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Business this week

Jul 8th 2004
From The Economist print edition

Yukos's woes

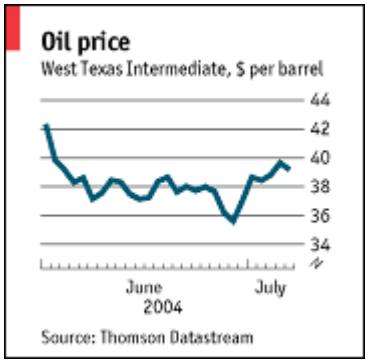
Yukos, Russia's biggest oil exporter, faced the prospect of bailiffs seizing its assets after it failed to pay $3.4 billion in back taxes. The company, which could eventually face a tax bill for some $10 billion, said that it might collapse unless a deal is reached with the government of President Vladimir Putin.

See article

Kenneth Lay, the former chairman and chief executive of **Enron**, was indicted for his role in the energy-trading giant's collapse in 2001. Some 30 people, including most of Enron's top management, have been charged with crimes connected with the firm's bankruptcy.

See article

Oil edged near to $40 a barrel. A recent price drop was reversed after further sabotage to pipelines in Iraq, concern over the fate of Yukos in Russia, strikes in Nigeria and signals that OPEC is unlikely to increase output at its meeting in August.



Green shoots

Philip Green increased his bid for Marks & Spencer, Britain's big clothes and foods chain, to £9.1 billion ($16.9 billion). The retailing tycoon claimed that M&S's largest shareholder was backing the improved offer. The company's board rejected the offer as inadequate.

The European Commission gave final approval for a *euro*2.5 billion ($3.1 billion) government bail-out of **Alstom.** In exchange, the commission has demanded that the troubled French engineering firm make divestments and find partners for its key businesses within four years.

EasyMoney?

EasyJet's founder, Stelios Haji-Ioannou, confirmed reports that he is considering taking the budget airline private. EasyGroup, which owns 41% of the carrier's shares, could pay £650m ($1.2 billion) to do so. The airline's shares have suffered since it issued a profit warning last month after fuel costs rose sharply.

See article

Delta Air Lines was reportedly ready to ask its pilots for concessions worth $1 billion a year. Delta says that it needs to cut spending by $2.5 billion a year in total to avoid bankruptcy. United Airlines, a larger American carrier, won a similar concession from its pilots earlier this year but may need to ask for more cuts to attract further financing.

Cut-price software

Microsoft plans to cut costs by $1 billion this year. According to an internal memo from Steve Ballmer, the software giant's chief executive, expenses have outgrown revenues for three years. He stressed the need to avoid “big company ills” by staying flexible and not losing touch with customers.

Wal-Mart appealed against the decision of an American judge to grant class-action status to a lawsuit alleging sex discrimination. The case, on behalf of up to 1.6m current and former female employees, could cost the world's leading retailer billions of dollars.

Pfizer announced plans to curb the cost of health care in America by expanding a scheme to offer discounted drugs to the uninsured and those on Medicare.

Apollo Management agreed to pay another private-equity firm, Kohlberg Kravis Roberts, some $655m to acquire **Borden Chemical** and expand its range of investments to include specialty chemicals.

Guta feeling

Guta Bank stoked fears of an impending banking crisis in Russia after it revealed that it did not have enough cash for withdrawals by private clients after a recent run on deposits. Several banks have suffered liquidity problems following a recent Central Bank decision to revoke the licences of Sodbiznesbank and CreditTrust.

See article

America's Securities and Exchange Commission widened its probe into the potential wrongdoings of **mutual funds**. It asked several big funds to give details of payments they had made to 401K retirement-plan administrators who had invested in their funds. The SEC is also investigating similar payments from mutual funds to brokerage firms that promote them.

Jordan's **Arab Bank** was hit with a $875m lawsuit from relatives of Americans killed or injured in Palestinian terrorist attacks in Israel. The bank is accused of “laundering” money through its New York branch as part of transactions that transferred money from Saudi Arabia to Palestinian militant groups in the West Bank and Gaza, including Hamas and Islamic Jihad.

America's Commerce Department made a preliminary ruling that would set tariffs of up to 93% and 113%, respectively, on **shrimps** imported from Vietnam and China. This followed complaints of dumping by American producers. Vietnam protested its innocence. Shrimps are its third-biggest export. Vietnam was hit by a similar American ruling on catfish imports last year.

See article

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The presidential race

Kerry's dream ticket?

Jul 8th 2004
From The Economist print edition

John Kerry chose the right running mate; but it will not solve the problems with his candidacy

Reuters

IN CHOOSING your vice-presidential candidate you are supposed to play safe. From their war rooms, the political pros point out that the last running-mate to have any real clout at the ballot box was Lyndon Johnson, who delivered Texas for John Kennedy back in 1960. Best to avoid inexperienced young senators (sooner or later Dan Quayle is mentioned). Best to choose a solid citizen who will not steal the limelight (step forward George Bush senior in 1980 or Dick Cheney in 2000). Best to choose a capable understudy who reiterates the main message of your campaign (Al Gore in 1992).

So why exactly does John Kerry's selection of John Edwards, a young-looking single-term senator from North Carolina who is as charmingly charismatic as his counterpart from Massachusetts is damnably dull, seem to make sense? The answer says quite a lot about how far the Democratic challenger has come in his campaign to unseat George Bush; and much more about how far Mr Kerry still has to go.

Consider the positives first. By choosing Mr Edwards, Mr Kerry has seized the momentum at a good time (see article). Just when Mr Bush's people were rather hoping that the generally better news from Iraq and from the economy would begin to push up the president's sluggish approval ratings, Mr Kerry has grabbed the limelight. With skill he may be able to keep the focus on his own campaign through to the end of this month's Democratic Party convention.

Mr Kerry has also broadened the appeal of his campaign. In theory, Mr Edwards gives the haughty Bostonian a chance in the South (though it would be a miracle if the Democrats picked up either of the Carolinas). In primaries across America his sunny Clintonian optimism went down well with the independent voters whom Mr Kerry needs to lure. Then there is class: Mr Kerry has only to open his mouth for voters to be reminded that he went to several expensive private schools and is married to a woman who could buy up any street and not notice; Mr Edwards is the son of a mill-worker who has become a millionaire lawyer. It is not just that Mr Edwards's “back-story” is more intriguing than Mr Kerry's, but also that he tells it far better: Mr Kerry can make a firefight in Vietnam sound like a mathematics textbook.

Now, argue the Democrats, this cannonball of southern charm can be fired at one of the weaker parts of the Republican rampart. Four years ago, Mr Cheney seemed a reassuring figure beside the young Texan governor. Now, like that other worrying old man, Donald Rumsfeld, he is associated with the administration's wilder escapades; nobody, for instance, has continued to insist that Saddam Hussein was linked to al-Qaeda more adamantly than the vice-president. For a populist jury-swayer like Mr Edwards, harrying Mr Cheney over that, and over Enron, Halliburton and the rest of his ties to big business will supposedly be child's play.

Yet boyish enthusiasm and populism also have their weaknesses. Despite serving on the Senate Intelligence Committee, Mr Edwards remains less than convincing on foreign affairs—something Mr Kerry pointed out in the primaries. In his role as the people's business-basher, he has also said some foolish things about trade, boasting about those trade agreements that he has opposed; it would be catastrophic if Mr Kerry went down this road, particularly given the protectionist sentiments amongst Democrats in Congress. As for the vice-presidential debate, Mr Cheney may fit the stereotype of good ol' boy capitalism, but Mr Edwards can also be caricatured as the slick trial lawyer—hardly a popular stereotype with business. Already, the Chamber of Commerce is threatening to give up its traditional neutrality and

support Mr Bush.

Truth be told, Mr Edwards shines as Mr Kerry's choice partly because of the alternatives. With Mr Kerry's overtures to John McCain, an independent-minded Republican who represented the true dream ticket, having seemingly failed, and Hillary Clinton biding her time till 2008, the decision apparently came down to Mr Edwards, Tom Vilsack, the interesting but somewhat obscure governor of Iowa, and Dick Gephardt, an old leftish warhorse with a proven record of being on the wrong side of just about every important economic argument of the past few decades.

Two painful truths

Worryingly, Mr Gephardt was the primary challenger to whom Mr Kerry seemed closest. Choosing as his running-mate Mr Edwards, with whom he clearly has less personal rapport, was a belated acknowledgement by Mr Kerry of two painful facts about his campaign. The first is that Mr Kerry is unlikely to get elected purely as the “Anybody But Bush” candidate. Plenty of Democrats loathe the president, which explains why Mr Kerry has raised so much money to fight him. But Mr Bush's base has remained solid throughout the bad news from Iraq, and many independents need convincing about the challenger. Despite the pasting he has received and his miserable approval ratings, Mr Bush still has a tiny lead, according to our first *Economist*/YouGov poll (see article).

This highlights the second, more fundamental fact: Mr Kerry has yet to articulate why he should be president. Back in 1992, Mr Gore was able to provide an echo for Mr Clinton only because there was an original song to repeat; they were both reforming New Democrats. Mr Kerry has come up with a few interesting ideas, notably on health care, and a few dodgy ones, notably on outsourcing; but the repeated image is of a man saying what he thinks his audience wants to hear. One reason why there is no danger of Mr Edwards contradicting Mr Kerry is because it is not clear what Kerryism is.

And on one fundamental point, those cynical political pros are right. Despite the hoopla this week, the choice of vice-president will not determine the election. Mr Quayle's much-ridiculed presence on the ticket did not stop George Bush senior winning in 1988. Even if Mr Edwards runs rings round Mr Cheney in their single debate, it will matter very little to voters when they decide whether they want to be led by Mr Bush or Mr Kerry. Bravo to John Kerry for making probably the best choice he could. But he still has a lot of work to do.

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Indonesia

A shining example

Jul 8th 2004
From The Economist print edition

Indonesia deserves great praise for its speedy transition from autocracy, through chaos, to democracy

ONE thing sceptics say about democracy is that it is well and good in orderly countries but impotent in the face of chaos. Three years ago, a newly democratic Indonesia seemed about to prove the point. Separatist and religious violence stalked the length of the archipelago; the rupiah was in free-fall; politics had descended to a pitiable level of squabbling and incompetence. The world's fourth most populous country, some foresaw, might come apart like a string of pearls; or, almost as bad, avoid disintegration only by the return of a brutal dictatorship such as that of Suharto, the general who was ousted by huge street protests in 1998. The parallels with the Balkans, where the fall of communism unleashed still greater horrors, seemed disquietingly apt. Unlike the Balkans, however, Indonesia contains 220m people, and is far and away the world's largest Muslim country: this would be chaos on an epic scale. In October 2002, such fears suddenly bulked much larger, when Islamist terrorists, linked to al-Qaeda, set off a bomb in Bali that killed more than 200 people.

This week things look wonderfully different. On July 5th, for the first time in their history, Indonesians voted to choose their president. The final result will not be known until late September, since a run-off between the two top candidates is now needed. But the election was free, fair, peaceful and, above all, conducted in a spirit of moderation that was remarkable in a country where democracy is only six years old. Megawati Sukarnoputri, the incumbent, urged everyone to accept the result, whatever it is, even though she seems unlikely to remain in office (see article).

If she does go, it will not be for any great misdeed, but because she is seen as having not been up to grappling with Indonesia's many problems. It is true that she is no intellectual, and no administrator either. But the verdict will be a little harsh. Her three years in office have been a valuable time of consolidation. With the exception of the continuing conflict in the province of Aceh, Indonesia is now more internally peaceful than seemed imaginable when she took over. The terrorists have not been eradicated, but they have been weakened by scores of arrests and a number of high-profile trials: tentative at first, the government has become increasingly confident in dealing with extremists. The improvement in economic stability has been almost as remarkable. Indonesia is showing steady growth of 4-5% a year, has a booming stockmarket and has won international praise for getting its government finances back under control. It would be wrong to overstate any of this. Indonesia is plagued by gigantic problems, high levels of corruption and of poverty being the two worst. But at least these are not existential. Miss Megawati has shown that Indonesia does not need a dictator as its president, even if that president is no longer to be her.

The man most likely to take her place is a former general, Susilo Bambang Yudhoyono, who this week emerged well ahead in the first round of voting, according to partial figures. Though he served under Mr Suharto, Mr Susilo is regarded as untainted, and he has worked well for successive democratic administrations. As a former security minister to Miss Megawati, he gets much of the credit for talking down some of the conflicts that bedevilled the early part of her term. If he has a weakness, it is that he has revealed little about what policies he might adopt if elected, campaigning more by exuding what appears to be a popular mixture of calmness, geniality and competence—plus a reasonable singing voice.

Who and what he isn't

More important than what the front-runner is may be what he is not. He is not, for instance, Wiranto, a much more controversial ex-general who was up for election and who has been indicted for crimes against humanity in East Timor. It seems that Indonesians, by a large margin, preferred a moderate military man to a nationalist throwback, even though Mr Wiranto had Indonesia's largest party behind him and Mr Susilo is backed by one he founded only this year. Nor did they care much for Islamists: two were also on the presidential ballot, but neither of them ever looked like making the run-off. And both of these, it should be noted, were moderates, opposed to calls for making Indonesia an Islamic state. Though there are plenty of groups that demand the introduction of *sharia* Islamic law, none of them was able to meet the minimal requirements for fielding a presidential candidate.

Indonesia's example ought to put paid to the notion, still common in the Muslim world and sometimes heard in the West, that democracy and Islam can never co-exist. One might very well argue that it shows the contrary: democracy is good for Islam. Whenever they are given a choice, Muslim voters—not just in Indonesia, but in Malaysia, India, Pakistan and arguably Turkey too—reject extremism. Once weighed in the democratic balance and found wanting, the more militant groups tend to lose much of their potency and support. It is the absence of democracy, as can been seen from Saudi Arabia to Uzbekistan, that breeds terror and subversion, and taints the reputation of what was once regarded as the most tolerant of religions. Malaysia is perhaps the most striking example of this phenomenon: only when Mahathir Mohamad tipped towards autocracy in the late 1990s did PAS, an Islamist party that demands the introduction of stoning and amputation, come close to posing a threat to secular government.

Even after this fine week for democracy, it would be dangerous to assume that Indonesia will never return to chaos if the economy sours, or if Mr Susilo fails too disgracefully in his stated aim of putting an end to corruption. But perhaps there is a lesson in Indonesia's experience not just for Islamic countries, but for one of Asia's other giants too. The party men who run China like to argue that democracy is unsuited to a poor, sprawling country that has no experience of it: chaos is what China's leaders say they fear above all. But it does now seem that Indonesia—a polyglot rag-bag of islands that emerged as a nation only through the accident of having been collectively administered by the Dutch—has given the world a powerful counter-example.

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Italy's troubled government

Cavaliere in a corner

Jul 8th 2004
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The Italian prime minister has done far too little to reform the economy

AFP

EVEN by his own standards, Silvio Berlusconi, Italy's prime minister, has had a tough few weeks. His party, Forza Italia, did badly in last month's European and local elections; last week it even lost an election in Mr Berlusconi's home bastion of Milan. The economy is moribund: Italy is vying with Germany for the title of sick man of Europe. This week Mr Berlusconi lost his finance minister, Giulio Tremonti, forced out by two of his coalition allies, the far-right National Alliance and the centre-right former Christian Democrats—and the country's debt was promptly downgraded by a big rating agency.

Mr Berlusconi's response to these troubles has been characteristically insouciant. He blamed the Euro-election reverse on ballot-rigging by the opposition. Instead of replacing Mr Tremonti, he has temporarily taken on the finance job himself (though he tried first to get Mario Monti, the EU competition commissioner, to do it). This week he was in Brussels lobbying euro-area finance ministers not to issue a formal warning to Italy for letting its budget deficit breach the stability-pact ceiling of 3% of GDP.

By promising more spending cuts, he won the day, though in truth only because so many other finance ministers are also breaking the rules. In all other respects Mr Berlusconi has lost. His oft-promised tax cuts are no nearer fruition—indeed, it was his partners' objections to them that led to Mr Tremonti's ouster. Italy's public finances remain a mess, with public debt standing at 106% of GDP and the deficit forecast to hit 4% of GDP in 2005. It was after Mr Berlusconi had taken over as finance minister that Standard & Poor's downgraded Italy's debt, the first time this has happened to a country in the euro. As the agency knows, Mr Tremonti held the deficit down only through temporary, one-off measures. He said himself this week: “It is difficult to manage the world's third-biggest debt pile without being its third-biggest economy.”

The Economist declared in 2001 (see article) that Mr Berlusconi was unfit to rule Italy because of his murky business past, his continuing judicial problems and his considerable array of conflicts of interest. The case that many Italians then made for giving him a chance despite all this rested on the belief that he would reform the economy and sort out the public finances. Yet three years on, he has achieved precious little in that regard. Instead, he has spent too much time dealing with his judicial problems—including pushing laws through parliament that seemed designed mainly to bolster his legal defences. And far from making good on his repeated promises to resolve his conflicts of interest, he has aggravated them. A new media law will allow his family's Mediaset empire to expand its reach. Now, as finance minister, he has become the main shareholder in all state companies, including RAI, the state television network whose chairman recently resigned in protest over political interference. In a formal sense, Mr Berlusconi today controls all of Italian television.

Given the fraught state of his coalition after Mr Tremonti's departure (see article), Mr Berlusconi's continuing promises of decisive action on the economy sound increasingly hollow. Earlier this year, Italy was picked out by the London-based Centre for European Reform think-tank as the biggest villain standing in the way of the EU's Lisbon agenda of economic change. Even those inclined to overlook conflicts of interest and judicial troubles must regret that Mr Berlusconi has failed to use his time in office to push the cause of reform in Italy.

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Russia's Yukos

An over-played hand

Jul 8th 2004
From The Economist print edition

Vladimir Putin's brutal tactics against the oil giant may be an ominous sign of weakness

Reuters

TWO weeks ago, Vladimir Putin reassured investors that his government was “not interested” in the bankruptcy of Yukos, one of Russia's biggest oil companies, which has spent a year fending off attacks by prosecutors and tax officials. But in the days after the Russian president's remarks, the attacks intensified: Yukos was ordered to pay $3.4 billion in back taxes by July 7th and threatened with another, similarly huge claim, while creditors declared the firm in default of a $1 billion loan. As *The Economist* went to press, with the tax-payment deadline past, Yukos was waiting for either an official response to its proposals for a deal, or for bailiffs to start seizing assets and selling them off to cover its debts (see article).

There would be a certain poetic justice if Yukos were to die, as it was born, through the aggressive interpretation of vaguely-defined laws. Its main shareholder and former boss, Mikhail Khodorkovsky—in jail on his own charges of tax evasion and embezzlement—has always insisted that the freewheeling ways in which he and other “oligarchs” acquired their companies in the 1990s were legal at the time. Indeed, the government itself helped to arrange the rigged auctions. Nobody doubts that Mr Khodorkovsky is now being punished for brazenly flouting Mr Putin's informal agreement with the oligarchs that they should not meddle in politics. And it seems clear that the Kremlin's ultimate intention is to make Mr Khodorkovsky and his partners give up their stake in Yukos.

Because of this, many foreign investors have until now seen Yukos's woes as something isolated: an inevitable stage in Mr Putin's attempts to wrest political power away from the oligarchs and to institute what he calls a “dictatorship of the law”. He clearly wants Russia to prosper, and understands the need for investment and economic reform. And the more he has tightened the state's grip on the media and political institutions, the more cheerily some have argued for the “benevolent-dictator” model: a heavy-handed and well-meaning ruler who can deliver reform, and prosperity, that much faster.

Yet the past few weeks have sown doubts, even among those who like the idea of a benevolent dictator. The blatant manipulation of the law against Yukos—its lawyers were given a few hours to review over 300 volumes of evidence—sets an example that politicians and prosecutors in other regions may now feel free to follow. Rumours that other oligarchs may be targeted next have made the financial markets jittery. And every other event that smacks of official whimsy, such as the threat earlier this year to suspend a leading mobile operator's licence, unnerves investors. This week the government claimed that America's ChevronTexaco plans a big Russian investment, but the firm gently dismissed the idea.

On top of that, Mr Putin's reforms are losing momentum. Liberalisation of the state-controlled gas and electricity sectors has been postponed. An overhaul of the army seems to have been abandoned. Mr Putin's shake-up of Russia's government has brought some departments nearly to a standstill.

One reassurance would be a quick and fair resolution of the Yukos affair, either by mutual agreement or by a sale of its assets conducted transparently. But a forced bankruptcy or a quick fire-sale to Kremlin favourites would suggest that either Mr Putin has ceased to care even about the appearance of propriety or that—as some observers suspect—things have spun beyond his control and he cannot keep the vultures away. Either would be an ominous development for Russia.

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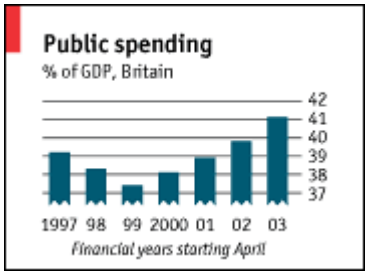
British public services

Has Tony wasted your money?

Jul 8th 2004
From The Economist print edition

Not entirely; but he has not changed public services enough either

Get article background



WHEN he came to power seven years ago, Tony Blair reckoned that his first job was to persuade voters to trust him with their money. So, for two years, he stuck to parsimonious Tory spending plans. By 1999, he reckoned that he had proved himself as sober as any taxpayer could wish, and that it was time to address voters' grumpiness with the state of public services. So the spending splurge began.

Since then, public spending has risen from 37.4% to 41.1% of a larger GDP. Health, which has been drenched in money, has seen its budget rise by an average of over 7% a year over the period. A healthy economy—for which the government can take some credit—has helped pay the bills, but taxes have had to go up and the budget deficit threatens to break Gordon Brown's self-imposed rules for prudent economic management. So next week's annual spending review will signal an end to the splurge in two years' time. Although health spending will continue to grow by over 7% a year in real terms until 2007, overall spending growth will fall from 6.6% in 2003 to an annual rate of 4% for two years and to 2.7% after that.

When voters come to think about the next election (which will probably happen next summer) the mess in Iraq is unlikely to be uppermost in their thoughts. They are more likely to be interested in whether the hospital will sort out grandma's hernia, and whether their children will get decently educated. The question that will chiefly determine how people cast their votes is: Has Labour spent all that extra money well?

I wouldn't start from here if I were you

The fundamentalist's answer is no. Anybody trying to design an ideal system for delivering public services would not start with the state as a near-monopoly provider and purchaser. Compared with other rich countries, Britain is at the extreme planned-economy end of the public-service model.

But, to the shame of the Conservatives, who had been in power for the previous 18 years, that was where the government did start. So the realist's answer would be: not too badly (see article) given some belated reforms, but not well enough to sustain the improvement without further changes.

Measuring the output of public services is always dodgy—how do you quantify the eagerness of a well-taught child?—but what measures there are support a lukewarm verdict. In health, for instance, while nominal spending increased by 10% in 2003, output increased by 4%. The improvement may be marginal, but voters seem to have perceived it: most now think the government is going to improve the health service.

That's what matters to the government right now. But the more important question for voters is whether, once the flood of money has stopped, the system will have changed enough to ensure that things go on getting better. And the contrasting stories of health and education suggest that it has not.

Health's main problem has been capacity. Waiting lists have been so long because of a shortage of doctors, nurses and hospital beds. Earlier this year the government started buying operations from the private sector in a big way. Foreign health companies are piling in, the capacity available to the NHS is

increasing and waiting times are consequently falling.

With education, by contrast, the problem is not so much quantity as quality. There's no overall shortage of school places: the shortage is of places in good schools. This week the government published plans to offer head teachers more independence from the state and stressing the importance of “choice” for parents. But if parental choice is to improve schools, good ones need financial incentives to grow and take over other schools. That's a step too far for Labour.

Given how deep Labour's hostility to the private sector runs, Mr Blair has done exceedingly well to pull the party as far towards the market as he has done. If his health reforms pay off, as they seem to be doing, they may give him courage to push on. He needs to, or he risks going down in history as a man who wasted a lot of money.

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Letters

Jul 8th 2004
From The Economist print edition

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For Europe to decide

SIR – I have no particular fondness for Jacques Chirac but you do him an injustice ("Still taking on the world?", July 3rd). It is not Mr Chirac who was amazingly rude but rather George Bush, who again could not help himself from trying to tell everyone what they should be doing. If Colin Powell had let it be known discreetly to members of the European Union that America would view Turkey's admission in a favourable light, that is one thing. But for America's president to declare, in the manner that he did, that Turkey has satisfied all the requirements for membership and should be admitted, invites the question of when America acquired any right to say whom the EU should allow into the club.

The situation is all the more inept because of the degree of mindless, bigoted objections I hear from European colleagues, friends and neighbours regarding the prospect of admitting a Muslim country into the EU, regardless of the merits of the case. In that light, and considering the incredible ill-will Mr Bush has created in Europe, his open and heavy-handed endorsement of Turkey could well be the kiss of death.

Michael Eustace Erwin
Paris

Good nature

SIR – You overlook an important and increasingly successful component of the World Heritage programme ("Ruins on the rack", June 19th). Complementing preservation of the magnificent cultural sites you mention, UNESCO encourages conservation of a tremendous inventory of natural World Heritage sites from the Galapagos Islands to Mount Kenya, where powerful models of public-private partnership are emerging. Recently, the United Nations Foundation and the Vodafone Group Foundation announced a $27m partnership that will support, in part, the establishment of a rapid-response facility for natural World Heritage sites facing imminent threat.

Multi-million-dollar partnerships with the private sectors have also been forged to help preserve sites in Central Africa and Brazil. The momentum for public-private co-operation to conserve the earth's natural wonders constitutes a bright new chapter in the history of the World Heritage programme.

Timothy Wirth
President
United Nations Foundation
Washington, DC

The PPPrice is right

SIR – Richard Cooper dissents from your view that purchasing-power parity rather than exchange rates should be used to measure world output and inter-country income spreads (Letters, June 19th). His nihilism demonstrates the need to continue your efforts to spread enlightenment. Within most countries, government statisticians provide regular estimates of aggregate output and expenditure in real terms, after correction for price changes over time. Virtually all economists regard these constant-price measures as key economic indicators—meaningful and indispensable for analysis of growth and fluctuations. The purpose of PPP measures is precisely analogous: to correct for price differences to

permit meaningful comparison of levels of real output and expenditure across countries.

Mr Cooper argues that inter-country variations in price and expenditure structure constitute an insurmountable obstacle to meaningful measurement of differences in the purchasing power of currencies. In fact these problems are similar in kind and no more intractable than those which arise in measuring inter-temporal changes in real output and expenditure. He is right to suggest that PPP is difficult to measure but wrong to suggest that measurement is impossible. Since the mid-1950s, there has been a massive effort by international agencies in co-operation with national statistical offices to deal with the kind of problem he raises. In my recent book on the world economy I used acceptable PPP expenditure converters produced by the OECD, Eurostat, UNSO and the UN regional agencies for 94% of world GDP, and short-cut measures from the Penn World Tables for another 5.5%. To compare the GDP of different countries by valuing quantities at prevailing exchange rates is no more meaningful than measurement of economic growth without adjustment for inter-temporal price change.

Angus Maddison
Chevincourt, France

Women at the top

SIR – You quote a former British managing director as saying that because of positive discrimination in appointing women "two-thirds of the men will say behind their hands that it's only because you're a woman" ("Sexism and the City", June 12th). Golly. Imagine what women have been saying openly for years when a man became managing director.

Felix Finch
Dutch Flat, California

Not-so-poor boy done good

SIR – Bill Clinton was not a "poor boy" in his youth, as you say in your review of his book ("Good ingredients, badly cooked", June 26th). His abusive stepfather (whose name he adopted, nevertheless) owned a car dealership. His mother was a registered nurse. This made the Clintons a modest two-income family. An uncle was a state senator. If Mr Clinton had been poor, his mother would have had to temper her addiction to the slot machines in Hot Springs and he would have been an unlikely candidate for his school band. Poverty would have forced Mr Clinton to spend his summers scrapping for spending money instead of meeting John Kennedy through the offices of Boys' Nation, an activity restricted to ambitious middle-class youth in those days.

I realise that to the sheltered Mr Clinton's upbringing looks "poor", but it was actually quite normal and bourgeois by American standards, let alone those of the South.

Mark Richard
Columbus, Ohio

Smart moves

SIR – I do not mind being called a "privacy advocate" (who would?) but I am disturbed to learn from your article on smart-tags that some research by my group is "scaremongering" ("The future is still smart", June 26th). I prefer to think of it as enabling. Smart tags hold promise but few people are trying to anticipate abuse and incorporate prophylaxis into the design. If you like smart tags, encourage us.

Peter Ladkin
University of Bielefeld
Bielefeld, Germany

Playing with his food

SIR – Why is Charlemagne obsessed with "potato-throwers" (June 12th)? As a flippant description of Andrzej Lepper and his Samoobrona party, it trivialises the seriousness of what they represent and verges on an ethnic slur to Poles. Assuming that name-calling is a new approach to evaluating political leaders, I would like to offer a few more food-derived epithets: "maize-stealing"—Robert Mugabe; "cabbage-irradiating"—Kim Jong Il; "pork-dispensing"—Junichiro Koizumi; "judiciary-roasting"—Silvio

Berlusconi; “date-breaking”—Paul Bremer; and “fruitcake-advised”—George Bush.

Dave Taggart
San Francisco

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Japan's foreign policy

From pacifism to populism

Jul 8th 2004 | TOKYO
From The Economist print edition

AFP

As Japan begins to stretch its long-unused military muscles, how far does it want to go and what can it do?

Get article background

IN DECEMBER 2001, with the world still shocked by the September 11th attacks, a North Korean spy ship sailed mischievously close to Japan. Although North Korean vessels did this often, Japan's coastguard had never done much about it. Japan is well known, after all, for its pacifist constitution. But this time was different. Japanese coastguard cutters gave chase, got into a gun battle that left some of their own crewmen wounded, and stuck with the fight until the spy ship exploded and sank in the East China Sea.

Apart from North Korea making trouble, everything about the clash was extraordinary. Although the spy ship was spotted within Japan's “exclusive” economic zone, it was outside Japan's more narrowly defined territorial waters. The official Japanese response to ambiguity is usually some sort of fudge. In this case, moreover, Japan had ample time to calibrate its reaction: the ship sank more than 24 hours after it had first been spotted. Nor did Japan offer a hint of regret. Even though the spy ship sank in China's economic zone, Japan's government claimed a right to salvage it, and stood by this decision. When the ship was raised, it was found to be loaded with spy gear and heavy weaponry.

The incident highlighted Japan's changing attitude towards its armed forces, which has gathered pace during Junichiro Koizumi's three-year stint as prime minister. The most visible sign of that shift occurred earlier this year, when Mr Koizumi sent more than 500 troops from its carefully-named Self Defence Forces (SDF), to help rebuild Iraq. Deploying them was a giant step historically, and not just because the force is sizeable and the theatre is dangerous. For the first time since the second world war, Japan has sent its soldiers abroad without the moral comfort of an international mandate.

In other ways, too, Mr Koizumi has sought throughout his tenure to test Japan's pacifist limits. Soon after the 2001 attacks, parliament passed a special law authorising ships from the Maritime SDF to help America's fleet in the Indian Ocean. The law restricted co-operation to refuelling and logistics, but Japan's navy, in effect, provided rear support for the invasion of Afghanistan. Last summer, parliament passed laws spelling out the government's powers in the event of an attack on Japan's territory. These laws had been discussed since the 1970s, but pacifist nervousness had prevented their enactment before last year. The prime minister has also called for changes to the constitution, including the pacifist restrictions in Article 9.

Land of the rising gun?

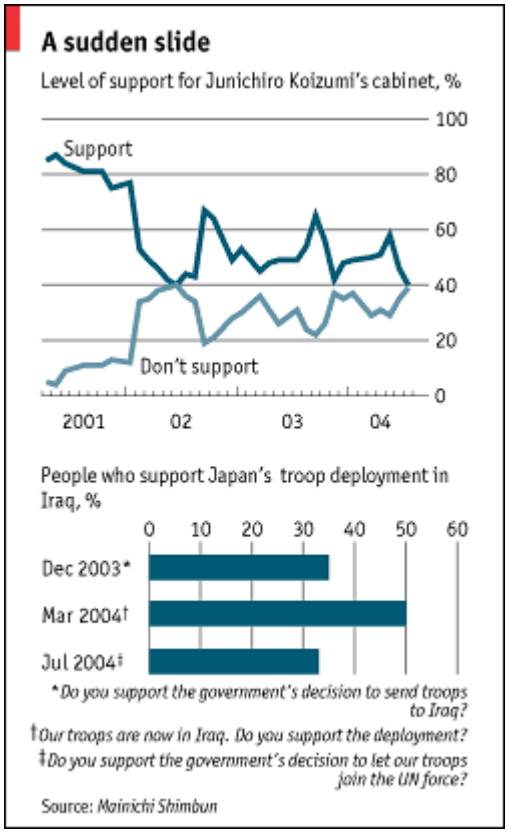
All this has delighted the administration of George Bush. America's alliance with Japan helps to shrink the Pacific, much as Anglo-American ties do the Atlantic. And because Asia is less coherent than the European Union, Japan's regional role is in some ways even more important to America than Britain's. In particular, America's 45,000 troops in Japan, and their related air and naval bases, matter more than its bases in any one European country. They not only protect Japan, but allow America to project strength across a region littered with potential hotspots. Many American officials reckon that as Japan gains confidence in its ability to use sailors and soldiers wisely, the alliance will grow more flexible and useful.

Although it pleases Mr Bush, however, Mr Koizumi's efforts to knock the rust off Japan's armed forces have rattled many others. Indeed, some of Mr Koizumi's critics seem unhappy precisely because America likes the idea. Others, both in and around Japan, take notice of Mr Koizumi's visits to the Yasukuni shrine, where more than a dozen war criminals are commemorated along with Japan's fallen soldiers. They detect signs of a resurgent right wing, and fear a return of Japanese militarism.

These criticisms are not convincing. Although Japan has indeed done much of what America wanted in Afghanistan and Iraq, it has hardly been bullied into it. Mr Koizumi has been as keen to lend a hand as Mr Bush has been to receive one. When their interests have diverged, Mr Koizumi has gladly stood up to his chum from Crawford. The Americans squealed last year when Japan ignored their sanctions on Iran and signed a deal to invest in its Azadegan oilfield.

Nor does Mr Koizumi's eagerness imply a sinister swing to the far right. His foreign policies reflect clear and reasonable national interests and draw support from the broad Japanese public, which shows little desire to remilitarise and start strong-arming neighbours. Mr Koizumi displayed his popular touch in May, for example, by visiting North Korea and trading food aid for the release of five children born to former abductees from Japan. This upset the nationalist right, but mainstream Japanese voters agreed that it was better to be pragmatic than tough. Mr Koizumi's poll ratings shot up by ten percentage points.

Since then, domestic issues, a looming election and other factors have combined to reverse that trend. Indeed, the poll numbers for Mr Koizumi and his cabinet, below 40% in some surveys, have rarely been lower (see chart). This week, as voters prepared to replace half of parliament's upper house in elections on July 11th, his ruling coalition seemed in danger of retaining its majority by an embarrassingly narrow margin. But the recent slide largely reflects a domestic row over pensions policy, combined with a sense that Mr Koizumi's political style has crossed the boundary from confident to cocky. It is not proof of a sudden and broad-based change of heart about foreign policy.



Voters do seem to have been dismayed by the prime minister's abrupt pledge, at the G8 meeting of rich countries last month, to include Japanese troops in a new multinational force in Iraq that has been endorsed by the United Nations. Since Japan has complex pacifist restrictions, the decision has important legal and democratic implications; but it will have little effect in practice on Japan's current mission, which involves helping to rebuild a quiet Iraqi town. The public reaction does not appear to reflect attitudes towards the deployment, since the mission will not change, so much as a sense that Mr Koizumi is cutting through delicate legal precedents without proper debate.

Far from being hijacked by a right-wing cabal, therefore, Japan's conduct of foreign policy is arguably growing more democratic. And the recent widening of the SDF's role, although driven by Mr Koizumi and viewed nervously by the public, reflects an interaction between his keen political instincts and broad popular attitudes. Those attitudes suggest that Japan is not so much flexing its muscles as it is stretching them after a long convalescence, to see whether they work and what they can usefully do.

The experiment began more than a decade ago. Many Japanese were humiliated by the first Gulf war, when western countries chastised Japan for failing to send troops, even though it had paid billions into America's war chest. In 1992, parliament passed a law allowing the SDF to venture abroad as long as its

troops were part of a UN mission and met several other criteria. Japan soon sent SDF troops to help UN peacekeepers in Cambodia (1992), Mozambique (1993) and East Timor (1999 and 2002); used them to extend relief to Rwandan refugees in 1994; and has had SDF members in the Golan Heights since 1996, as part of a team of UN observers.

Self-Respect Forces

Most Japanese are proud of these missions, but this hardly reflects a popular urge to redefine their country as a military power. The prevailing Japanese attitude towards using force is closer, for obvious reasons, to the dominant view in Germany. Whereas many Americans, Australians and Britons look on war as a terrible option, which at times must be weighed against other nasty outcomes, most Germans and Japanese came to a simpler conclusion after the second world war: that war is always wrong.

That pacifist streak, along with a desire to avoid criticism, is reflected in the limits that the 1992 law placed on Japanese peacekeeping missions. These state that the SDF can be sent only when a ceasefire is in place and when all parties to a conflict agree that Japan can take part. The law also strictly limited the use of weapons to “the minimum necessary to protect the life or person of the personnel”.

These rules seemed a reasonable extension of Japan's previous post-war foreign policy, which had used generous aid and tireless self-promotion of Japan's “peace-loving” credentials to win friends and influence governments. Yukio Okamoto, a former adviser to Mr Koizumi on foreign affairs, says that the restrictions led his countrymen to view the Japanese troops as “NGOs in blue helmets”: harmless aid workers with a UN stamp of approval.

Despite these pacifist leanings, however, there are huge differences between Japan on the one hand and Germany on the other. One is obvious: Japan faces clear threats. For Germany, the end of the cold war removed the Soviet threat, and it now faces little risk of a military attack. In Japan, however, the cold war gave way to a new danger: North Korea.

The discovery in the early 1990s that North Korea was developing plutonium, which could be used to make nuclear warheads, got the public's attention. Those fears grew after North Korea's shocking decision to test a medium-range Taepodong missile in 1998, lobbing it over Japanese airspace into the Pacific Ocean. Even before Mr Koizumi entered office, therefore, Japan had taken steps to deal with the North Korean threat. Further signs of bad behaviour during his term have strengthened the public resolve—not least North Korea's admission (since denied), in 2002, that it had violated a 1994 agreement by trying to enrich uranium.

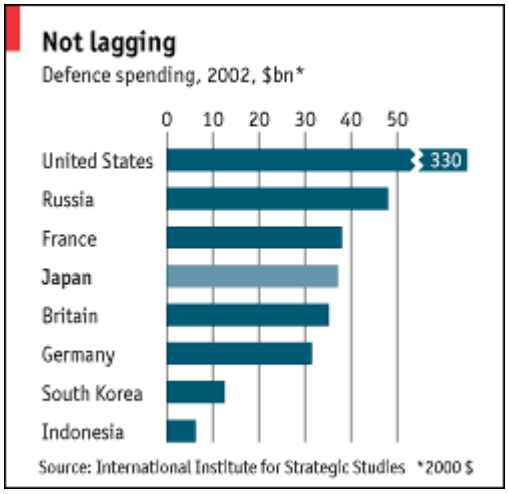
Japan has responded stiffly. Last year it launched the first spy satellites in its history to get an independent look at North Korea. It has joined the Proliferation Security Initiative, a multilateral effort to interdict North Korean ships carrying weapons and contraband, and thus to eat into the regime's hard-currency earnings. In February, parliament passed a law allowing the government to impose economic sanctions on North Korea—including banning cash remittances—unilaterally, and without any UN resolution. Another law allowed the government to deny port calls by the North Korean ferry that retrieves hard currency from criminal groups in Japan. And Japan is now in talks to quicken the rollout of a proposed missile-defence system, on which it is co-operating with America.

The public clearly favours Mr Koizumi's tough stance towards North Korea. When he needed a new secretary-general to run last year's general-election campaign, he chose Shinzo Abe, a youthful politician who had made a name for himself with his hawkish views on Kim Jong Il's regime. The North Korean threat, by highlighting the importance of the alliance with America, partly explains why much of Japan's public supports the sending of the SDF to Iraq, even though that mission stretches the pacifist limits.

That, however, is only part of the story. Besides having North Korea next door, Japan also differs from Germany, and, indeed, other European countries, in other important respects. For both Germany and France, one of the easiest ways to strut a little taller in the world is occasionally to get up America's nose. France can do this easily, given its permanent seat on the UN Security Council. Working in tandem, moreover, France and Germany together can exert a strong influence on the European Union, sometimes trying to steer it in ways that frustrate American goals.

Japan has no such diplomatic clout—and only three conceivable ways to gain any in the near future. It could get a permanent seat on the Security Council, which it has sought for years and shows

few signs of obtaining. It could behave in Asia as France does in the EU, putting its weight behind regional initiatives that exclude non-Asian countries. But even if it could pull this off—which would be highly implausible in the face of regional rivalries—it would damage its own economy, which depends heavily on globalisation. Since these two ideas are non-starters, the most sensible way for Japan to gain influence is to start putting its substantial military resources (see chart) to work multilaterally, and to make genuine security contributions as often as they are called for.



Many Japanese diplomats and foreign-policy experts argue that Japan already carries weight on the global stage. It has been one of the world's top two official aid donors, along with America, since the 1980s, spending ¥500 billion ($4.6 billion) a year. It takes part in every important international gathering, and Japanese diplomats rarely say the wrong thing. Yet it is significant that in "Plan of Attack", Bob Woodward's detailed account of the preparations to invade Iraq, Japan's role in the convoluted diplomacy goes more or less unmentioned.

How to lay low and influence people

Most Japanese are not so keen for their country to loom large, however, that they are willing to scrap their pacifist principles altogether. Japan's overall foreign policy remains, at root, risk-averse. This is a global economic power that relies heavily on reliable imports of energy and unfettered access to world markets. It wants to stay on good terms with as many countries as possible. Regionally, its main aims are to avoid losing out to China on trade deals and to manage the alliance with America so as to fend off would-be aggressors.

The echoes from the Gulf war, however, have given that risk-aversion a new twist. Although Japanese voters clearly prefer safe missions with little chance of shooting, they have been so scandalised by foreign criticism that they are willing to back SDF deployments, when reassured that these are legal and proper.

AP

Proud to fly the flag

This fear of humiliation was on display in April, when some Japanese do-gooders were kidnapped in Iraq and later released. The psychiatrist who met them on their return told the *New York Times* that their most stressful moment came not when they were kidnapped or had knives at their throats, but rather when they had to face their countrymen back home. Most Japanese were angry over the trouble and embarrassment the hostages had caused.

As Japan's security policy evolves, these same factors—the North Korean threat, the American alliance, the Japanese public's changing perceptions and Mr Koizumi's popular touch—will remain the ones to watch. The most immediate risk to Mr Koizumi is the fallout if his party does poorly on July 11th, as the polls suggest it will. Over the past three years he has honed his populist approach by strengthening the role of his own office and the cabinet in making policy. This allows him to seize chances as they come along. If his popular aura is dented by a weak showing on election day, he may struggle to regain his foreign-policy footing.

As always for Japan, presidential elections in America will also bear watching. From the Japanese point of view, the most important difference between a President John Kerry and Mr Bush would involve North Korea, with which Mr Kerry has said he will talk bilaterally. But while any easing of tensions with North Korea, or some sort of diplomatic fudge, would affect Japan's posture towards the regime, the public will no doubt remain wary.

A more important change will come, sooner or later, when Mr Koizumi leaves office. Arguably, Japan has never had a prime minister like him, at least in style. Yet he could be replaced by anyone ranging from a dull member of the LDP gerontocracy to his hawkish and popular young protégé, Mr Abe; or from a nationalist governor such as Shintaro Ishihara, to a socialist one such as Yasuo Tanaka. Meanwhile, the

opposition Democrats, who are keen to distance Japan from America a bit, have at last managed to establish themselves as legitimate contenders for power.

The best guide to foreign policy in post-Koizumi Japan, therefore, lies in those popular attitudes that he has so skilfully tapped. Where they are clearly threatened, such as by North Korea, Japanese voters have certainly lost their pacifist inhibitions. After salvaging the North Korean spy ship, the government put it on display near Tokyo Bay so that the public could go and marvel at the menace their sailors had confronted. Japan's annual white paper on defence, published on July 6th, suggests that the country also needs to keep a close eye on China, a possibly dangerous rival in areas other than trade.

Whether the public will keep backing missions outside the region, however, will hinge on events. By choosing a series of safe missions, Mr Koizumi and his predecessors have helped mould the popular mood in favour of more SDF deployments. Should one of the missions turn bloody, however, there is no telling how the Japanese will react.

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The Democratic ticket

Gee up!

Jul 8th 2004 | WASHINGTON, DC
From The Economist print edition

Democrats think John Edwards is a great campaigner who will improve John Kerry's presidential chances. That looks half right

Get article background

IN 1997, a Democratic political consultant in North Carolina got a phone call from an unknown lawyer in Raleigh. The caller had never run for public office, had not always voted and was unsure whether he initially registered as a Democrat or Republican. But the previous year his 16-year-old son had been killed in a car crash and the personal tragedy had turned his mind to politics. He asked about running for a Senate seat. The state Senate, assumed the consultant. No, came the ambitious reply, the United States Senate.

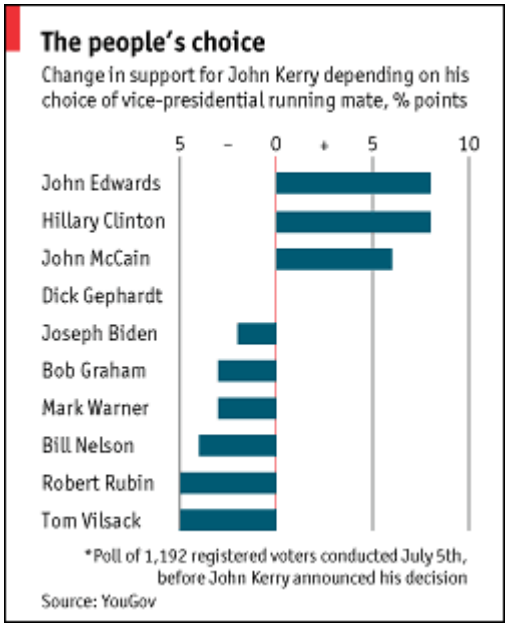
A year later the man had toppled an incumbent Republican in a solid red state. After two further years, he was on the short list as Al Gore's running-mate. Now, less than six years after his only election victory, John Edwards is John Kerry's (and most of the Democratic Party's) choice as vice-presidential candidate, confidently striding past Dick Gephardt, a former Democratic leader in the House.

America seems to produce two kinds of politician. One slogs away for years, clawing his way to the top. Mr Kerry (19 years in the Senate) and Mr Gephardt (27 years in the House) are prime examples. The other soars effortlessly up on the back of a compelling personal story or manner. Mr Edwards joins the ranks of George Bush and Arnold Schwarzenegger in this second category. In this respect, as in others, he balances the Democratic ticket.

Mr Edwards is a southerner to Mr Kerry's Yankee. He is the son of a mill-worker, not a scion of the Forbes and Winthrop clans. He was educated in public schools in the Carolinas, not in Switzerland and Yale. He is 51 and looks younger. The 60-year-old Mr Kerry looks like a portrait of himself by Edvard Munch. Mr Edwards can create an emotional bond with his audience. Mr Kerry could put a hummingbird into a coma.

For all these reasons, Mr Edwards promises to be a good campaigner, strong where Mr Kerry is weak. The presidential nominee is respected but not greatly liked by his party. Mr Edwards is one of its stars. An internet poll of 1,192 Americans for *The Economist* taken on the eve of Mr Kerry's decision by YouGov, a British-based pollster, showed Mr Edwards would increase the ticket's vote by more than any plausible rival; his only competitors were Hillary Clinton and John McCain, both of whom had ruled themselves out (see chart). An Annenberg poll shows his

favourable ratings are almost twice his unfavourables—a healthy balance.



Mr Edwards's Senate victory and his record during the primaries suggested he is more successful than Mr Kerry with rural and small-town voters—exactly the people who matter in mid-western battleground states. Mr Edwards put in electrifying performances in black churches; Mr Kerry (perhaps unfairly) has been criticised for taking black voters for granted. Mr Kerry scores disproportionately well among young and older voters but badly among 30-to-65-year-olds; perhaps Mr Edwards can close that curious age gap.

Vice-presidential picks rarely deliver blocks of votes, and Mr Edwards will not hand over the South, gift-wrapped, to Democrats. But the list of battleground states has been lengthening lately; in his home state of North Carolina, for instance, which Mr Bush won by 13 points in 2000, the Republican lead is down to five.

At the very least, Mr Edwards should force Republicans to spend more money winning the South than they otherwise would. He will make some of the outer ring of southern states that Bill Clinton won—Arkansas, West Virginia, Florida, Louisiana—more competitive. And by giving Democrats a candidate at the top of the ticket that southern politicians do not want to run away from, Mr Edwards could increase his party's chances in five local Senate contests—Florida, South and North Carolina, Georgia and Louisiana.

Above all, Mr Edwards strengthens three electoral messages that are vital to Democratic victory but for which Mr Kerry is a poor messenger. One is the need for change. Long public service makes Mr Kerry the standard breed of Washington insider (the same would have been said of Mr Gephardt). Mr Edwards's relative lack of experience—in most ways a drawback—sharpens the message of change.

Next, thanks to his smile, accent and "Two Americas" stump speech (one for the rich, one for the rest), Mr Edwards somehow manages to be both a populist and sunny at the same time. This may blunt the Republican charge that Mr Kerry's campaign is "pessimistic" (a cardinal sin in American politics).

Third, that same sunny populism has also allowed Mr Edwards, unlike Mr Kerry, to articulate a domestic-policy message that resonates with what Mr Clinton used to call the "forgotten middle class". In the summer of 1992, the last time America was recovering lumberingly from a recession, Mr Clinton was as much as 15 points ahead of the then President Bush on public perceptions of handling the economy. Mr Kerry is only five points ahead. Democrats hope some of Mr Edwards's magic might rub off on their top man.

Judging by the initial brouhaha—both from Democrats and the media—it might appear as if this is happening already. Because the party is unusually united this year, Mr Kerry had a free choice of running-mate: he had no factions to appease or confront. He won praise for picking the rank-and-file's favourite. Interestingly, he also picked the candidate who helps him most in the campaign rather than with governing afterwards. To his credit, Mr Kerry is realistic about his personal weaknesses and unafraid of being upstaged by a charismatic running-mate.

The manner of his "first presidential decision" (as Mr Clinton called the choice of running-mate), also tells you something about how Mr Kerry might govern if elected. He consulted extensively, getting every possible point of view several times over. He then kept his decision secret to the last moment. The *New York Post* even announced he had chosen Mr Gephardt on the very morning when he announced he had picked Mr Edwards.

This accords with Mr Kerry's modus operandi in the Senate. He used to thrash out issues to death with his staff—yet they were often unsure when he strode to the Senate floor which way he was going to vote. Whether this manner of making decisions would help or hinder him as president is unclear. But it worked brilliantly as a way of maximising the publicity of choosing a running-mate.

Getting the right man

So the initial reaction to the choice was positive. But it is not certain how long the glow will last. Mr Edwards is a good campaigner, but not as good as his fans believe. Though he is a member of the Senate Intelligence Committee, in other respects he has about the same experience in foreign policy as Mr Bush had four years ago—that is, after September 11th, not enough. Mr Kerry seems to be gambling that his own experience in Vietnam and the Senate means he does not need any help to debate national security.

The evidence for Mr Edwards's vaunted ability to attract moderates is also surprisingly thin. In the primaries, he certainly attracted rural and small-town voters and did well among independents. But it turns out that these people were not necessarily moderate sorts.

According to Larry Sabato of the University of Virginia, their views were actually quite left-wing, as might be expected in a Democratic primary. It is possible they liked Mr Edwards not because they thought he was rather conservative but because they saw him as rather leftish—something that his anti-trade rhetoric, his opposition to legal reform and his voting record in the Senate all suggest. Republicans are already trying to portray the Democratic ticket as the most left-wing in history. That looks a stretch, but Mr Edwards's appeal to rust-belt cultural conservatives must, for the moment, be considered unproven.

His background as a trial lawyer may not hurt him directly (opponents in North Carolina were never able to persuade voters that arguing a legal case for small children injured by corporate negligence was such a bad thing). But it has incensed business groups. The president of the National Association of Manufacturers says Mr Edwards “demonstrates conspicuous hostility to manufacturing and business.”

Democrats are looking forward eagerly to the vice-presidential TV debate, thinking their sunny candidate will dispatch Dick Cheney, the evil cyborg. They may be disappointed. Mr Cheney will seek to present the contest as one between someone who is experienced in national security and pro-business (even if that business was Halliburton) and Mr Edwards, who is neither of these things. In normal circumstances in America, whom would you expect to win such a debate?

Most important, even if Mr Edwards were the paragon that Democrats imagine, it is not certain he could make anything other than a marginal difference. Voters pay attention to the vice-presidential contest at only three points during the election: now (when the announcement is made), at the convention and during the vice-presidential debate. This is not often enough to make a real difference to perceptions of the man at the top.

So if Mr Kerry remains the political equivalent of Valium, Mr Edwards cannot rectify that. He might even make things worse by showing him up. And if Mr Kerry cannot create enthusiasm for his domestic-policy agenda (and, so far, he hasn't, at least compared with Mr Clinton), Mr Edwards cannot do it for him, however often he gives that “Two Americas” speech.

The best that the running-mate can do is increase the public standing of the ticket for a few weeks after he or she is selected, ie, around the time of the party convention. This “post-convention” bounce is then offset to a greater or lesser extent by a bounce on the other side. After things have settled down in early September, the party that is then in the lead more often than not goes on to victory.

This year, the Democrats' post-convention bounce will matter more than usual because it will test the idea that Mr Kerry ought to be doing better than he is (on the grounds that Mr Bush has taken such a drubbing in Iraq). At the moment, most polls show the horse race roughly even (our YouGov poll puts Mr Bush a point up; a recent CBS poll puts him one down). That has been excusable so far because all the attention has been on the president. But with the choice of running-mate, the focus shifts to the challenger. According to Karlyn Bowman, a poll watcher at the American Enterprise Institute, the “post-convention bounce” usually increases a candidate's score by five to ten points.

Using that yardstick, if Mr Kerry's standing in August, after his convention, is at the bottom of that range, it will be fair to say he is in trouble. If it is up around ten points, and especially if Mr Bush does not then bounce back, Mr Kerry should have cause for optimism. And a small part of the credit will belong to his choice of Mr Edwards this week.

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The economy

Running out of steam

Jul 8th 2004 | WASHINGTON, DC
From The Economist print edition

Is the recovery losing momentum?

Get article background

PITY the Republicans. No sooner had America's jobs figures become rosy enough to brag about in campaign ads, than the pesky statistics stopped playing ball. According to numbers released on July 2nd, only 112,000 new non-farm jobs were created in June, far fewer than in each of the previous three months and less than half what analysts were expecting. After rising for four months, jobs in the politically sensitive manufacturing sector fell. The average work-week shortened and the unemployment rate is stuck at 5.6%.

Democrats quickly pointed out that America has lost more than 1m jobs since George Bush took office. The president himself claimed that he had been looking all along for “steady, consistent growth” rather than “boom-or-bust”. Don Evans, his commerce secretary, said new jobs had been created in each of the past ten months, including June. “The trend is our friend,” he argued.

But is it? That depends on whether June's figures were a one-off, or whether they mark a broader slow-down. It is always a mistake to read too much into one month's jobs statistics. And June had particular oddities. The fall in the average work-week, for instance, may have been influenced by the fact that many workers had the day off on June 11th for Ronald Reagan's funeral, a day that happened to be during the statisticians' survey week.

That said, the number-crunchers also revised down the jobs figures for April and May a bit. And other evidence suggests America's economy may be cooling somewhat. Durable goods orders (admittedly yet another highly volatile indicator) fell in May for the second consecutive month. Vehicles sales were decidedly lame in June. Measured at an annual rate, only 15.4m light vehicles were sold in June, a sharp fall from the 17.8m rate in May. And, perhaps most significant, several big chain stores, including Target and Wal-Mart, warned that June would be weak.

It is not all bad. For instance, consumer confidence looks robust (the Conference Board's index rose to 101.9 in June, its highest level in two years). But for Mr Bush, even conflicting signals look dangerous. For the past few months, his campaign has been frustrated by how little his poll ratings have benefited from a string of uniformly rosy economic statistics. If the economic numbers are less rosy, then the poll numbers could yet go down.

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The electoral week

On the trail

Jul 8th 2004
From The Economist print edition

Give them what they want

"I trust that met with your approval."

John Kerry tells cheering supporters that John Edwards is his veep, July 6th

Pre-emptive strike

"I am both honoured and flattered that you are seriously considering me for your running mate...I respectfully remove myself from the selection process."

Bill Richardson takes himself out of the VP stakes before he doesn't get selected. Albuquerque Journal, July 2nd

Rupert Murdoch on line one

"We unreservedly apologise to our readers for the mistake."

The New York Post editor-in-chief on his paper's headline announcing exclusively that Mr Kerry had selected Dick Gephardt. New York Post, July 6th

Rupert Murdoch on line two

"John Kerry's 757 was in hgr 4 pit tonight John Edwards vp decals were being put on engine cowlings and upper fuselage."

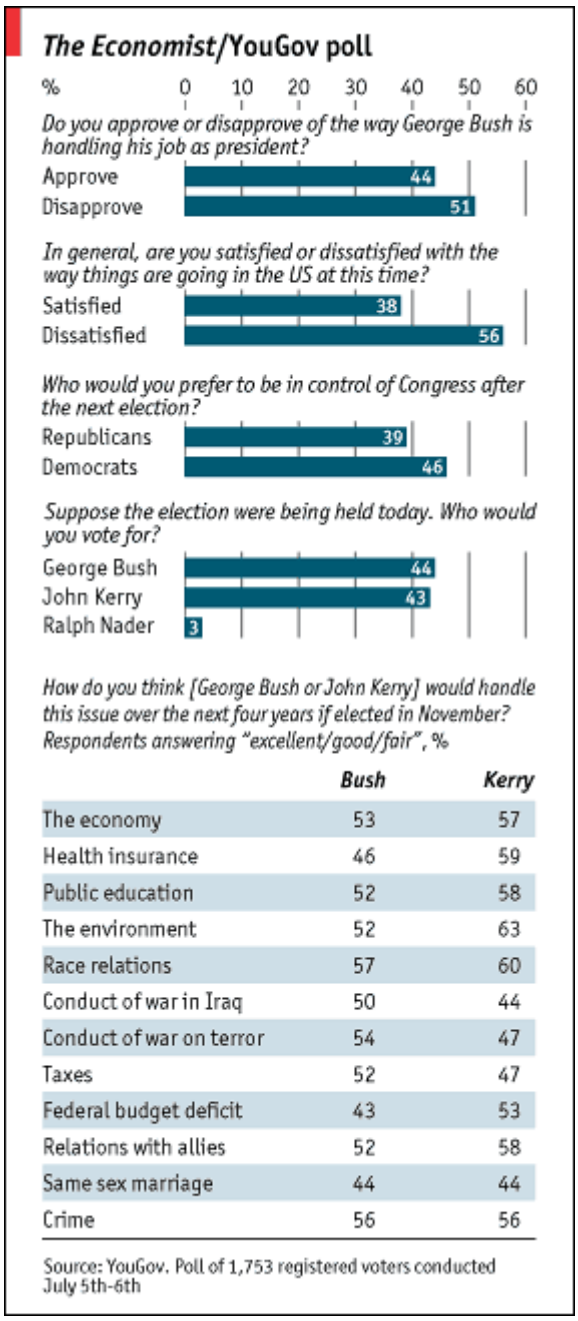
A posting on www.USaviation.com at 9.44pm on July 5th, 12 hours before the announcement. talkingpointsmemo.com

A new venture

The table below shows data from the first *Economist*/YouGov poll,

which will now run weekly until the election in November. YouGov, a British pollster, has recruited an online panel of 10,000 Americans, which will grow to 20,000 over the course of the poll. The full survey can be found at

www.economist.com/yougov.



Conspiracy theory

"Republicans own the movie chain."

A disgruntled customer's explanation for why a Virginia cinema showed "Fahrenheit 9/11" with no sound. Washington Post, July 2nd

John of Arc

"By spreading heresy, he is endangering not just mine but every Catholic's possession of the faith."

A lawyer has filed heresy charges against Mr Kerry with the Archdiocese of Boston, because he supports abortion rights. Washington Times, July 1st

Church times

"Efforts aimed at transforming houses of worship into campaign offices stink to high heaven."

Rabbi David Saperstein of the Religious Action Centre of Reform Judaism on the Bush campaign's attempt to use churches to reach voters. July 1st

That Florida feeling

“Of course, there's going to be people on there who are not really felons...Does it bother me? I'm sure there are other people like that on there.”

The Florida Department of State on a list of 47,000 felons denied the right to vote. South Florida Sun-Sentinel, July 2nd

Ouch!

Running in Heels is attempting to register voters by arranging singles parties and offering bikini waxes and yoga classes. The organisation also sells “Bush-free zone” women's underwear.

Time, July 12th

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Anti-dumping rules

Shrimp wars

Jul 8th 2004 | NEW ORLEANS
From The Economist print edition

A very big row over very small creatures

THE ports along the lower Mississippi River are among the busiest in the country, but Louisiana has a mixed-up approach to trade. It protested louder than most about the steel tariffs imposed by the Bush administration in March 2002: imports of steel at the Port of New Orleans dropped by half. Yet other mainstays of its economy are propped up by trade restrictions: subsidies for rice and sugar, and tariffs that keep out Vietnamese catfish and Chinese crayfish meat.

Now more tariffs are coming. The Southern Shrimp Alliance, a group of shrimp fishermen and processors from eight states, has long accused its rivals in Thailand, China, Vietnam, India, Ecuador and Brazil of dumping their produce on the American market. In December it urged the government to impose tariffs on imports from these countries, which now account for two-thirds of the American shrimp market.

In February, America's International Trade Commission ruled that these six foreign countries had indeed injured the domestic industry. And on July 6th, the Commerce Department, concluding that China and Vietnam were selling the little crustaceans below fair value, imposed anti-dumping duties of up to 93.13% on shrimp from Vietnam and up to 112.81% on shrimp from China. Decisions on the other four offenders will come later this year.

Louisiana is the largest producer of warm-water shrimp in the country. Amid the bayous and marshes near the Gulf of Mexico, trawling for shrimp has been a way of life for generations. But it is an increasingly precarious existence. Kim Chauvin, an activist who lives in a small town that shares her surname, sells the shrimp that her husband and her two sons catch. Her records show that the going price for one category of medium-to-large shrimp has plunged from $6.45 per pound in 2000 to $1.80 this spring.

In response she has taken marketing courses, invested in a costly new freezer and started to work out faster ways of transporting shrimp. Even so, her business, which in 2000 made about $60,000 after operating expenses, was $55,000 in debt by March. “I don't understand how they expect Americans to compete with countries that have slave labour and pay people 33 cents an hour,” she says.

Wally Stevens, the chief operating officer of Slade Gorton, a seafood distributor in Boston, argues that the damage is self-inflicted. The American Seafood Distributors Association, of which Mr Stevens is president, maintains that farmed shrimp is more consistent in size and quality than domestic shrimp. He also says the domestic industry has tried to compete on price alone—impossible, since trawlers and fuel are so expensive—instead of marketing to a niche. The sort of sophisticated consumers who seek out boutique pinot noirs from Oregon and artisanal cheeses from Vermont would presumably pay a little extra for wild-caught Louisiana shrimp. The shrimpers reply that better marketing alone won't keep them in business, and that a big advertising blitz would eat up money few of them have.

Will Tuesday's decision stand? Vietnam (which is already protesting against the catfish tariffs) has said it will appeal. The duties are likely to raise the price of shrimp to the American consumer by 44%, but trade rows do an administration little harm in an election year. And the clamour is growing for protection for other industries. Louisiana's crab fishermen are gearing up to follow the shrimpers' example.

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A new light railway

Onward, Swedish socialists

Jul 8th 2004 | ST PAUL
From The Economist print edition

A debate about transport reveals old divides in Minnesota

RARELY is travelling in the crowded Twin Cities a pleasure. Yet on June 26th it seemed to become so for the 95,000 people who rode the new light-rail line on its opening weekend. Fifty years since the demise of the streetcars, they had the chance to see Minneapolis from a train. The Hiawatha Line, which cost $715m, will eventually run 12 miles from the city centre to the airport.

The Twin Cities have been flirting with light rail since the 1970s. The project never left the station in part because various governors opposed it, but also because it reflected a debate about Minnesota's identity.

Supporters of the project enthused, in the usual way, about reordering the urban landscape and cherishing the environment. To its opponents, however, light rail epitomised an outdated urban liberal penchant for social control, dense living and an irrational Europhilia—all the sort of things that left-leaning Minnesota used to be proud of. The conservative Taxpayers League of Minnesota, which carries much weight with conservative Republicans (including the state's governor, Tim Pawlenty) pointed out that light rail cost far more than roads.

The biggest battle came over congestion, which is growing at a faster pace than in any other city except Atlanta. Light-rail enthusiasts said their project would ease it; conservatives countered that most studies show otherwise. The Heritage Foundation, for instance, argues that congestion has increased by more than 20% in cities that have brought in light rail.

But if light rail is “social engineering”, its supporters claim that it is justified, just as the Interstate highway system was justified after the second world war. They believe that, just as those new highways encouraged suburban living, so federal and state government must create a “settlement framework” for the 21st century that encourages people to live closer to the cities and to break their dependence on cars.

Light-rail riders in Minneapolis are projected to reach 19,300 a day by 2005 and 24,600 by 2020. But these estimates may be conservative. When St Louis introduced light rail in 1993, the number of actual passengers was more than three times the projections. Denver, Portland, Dallas, San Diego and Salt Lake City have all seen passenger numbers higher than anyone dreamed of.

But the proof of light rail's success will be as much around the tracks as in the cars. The Twin Cities Metropolitan Council predicts that light rail will spur the building of more than 7,000 housing units and 19m square feet of office space, almost as much as downtown Minneapolis has already. Mixed-use buildings are now rising fast in and around the light-rail stations. It might have happened anyway; but it looks as though the return of rail has given the Twin Cities something of a boost.

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Swing states: Washington

Diversionary attacks

Jul 8th 2004 | SEATTLE
From The Economist print edition

John Kerry should win Washington state. But how much time and money will it cost him to do so?

“YOU can see all the voters you need from the top of the Space Needle,” is how the late Henry “Scoop” Jackson, a Democratic senator for three decades, once described Washington's political landscape. The geography still holds: in a state of 5.9m the Seattle landmark overlooks more than half the population, from Microsoft millionaires to Boeing assembly workers. They live west of the mountains that psephologists call “the Cascade curtain”, and they traditionally vote for Democrats, in contrast to the less numerous rural Republicans east of the Cascades.

Washington's governor, both its senators and six of its nine congressmen are Democrats. In 2000, Al Gore beat George Bush by a handy 5.6 percentage points, despite Ralph Nader getting 4% of the vote.

Some swing states will remain toss-ups right up to election day in November; Washington isn't—or, from John Kerry's point of view, shouldn't be. Both sides still consider it a battleground state for the moment and are advertising accordingly; but if Mr Kerry is to have any chance of getting into the White House, he must try to move the state over the summer from the “Kerry-leaning” column to the “safe Kerry” one. If not, in the final phase of the campaign, he will have to spend time and money that would otherwise go to Ohio or Florida.

In 2000, Mr Bush popped up to steal a few once supposedly Democratic-leaning states—notably West Virginia. And his surrogates are talking tough in Washington. Chris Vance, chairman of Washington's Republican Party since 2000, trots out two of the usual arguments: the economy is improving, and so is the situation in Iraq. But then, citing extended Medicare, the proposed guest-worker programme for illegal Latino immigrants and extra funding for education, he adds an unusual third reason: “George Bush's record is not that conservative...There's something there for everyone.”

Mr Bush will doubtless try to burnish his compassionate-conservative credentials at the Republican convention. But Mr Vance's pitch probably has less to do with the product than the audience. Washington state, as Mr Vance admits, is one of America's most secular, least overtly patriotic places. It is “culturally different from other parts of the country”.

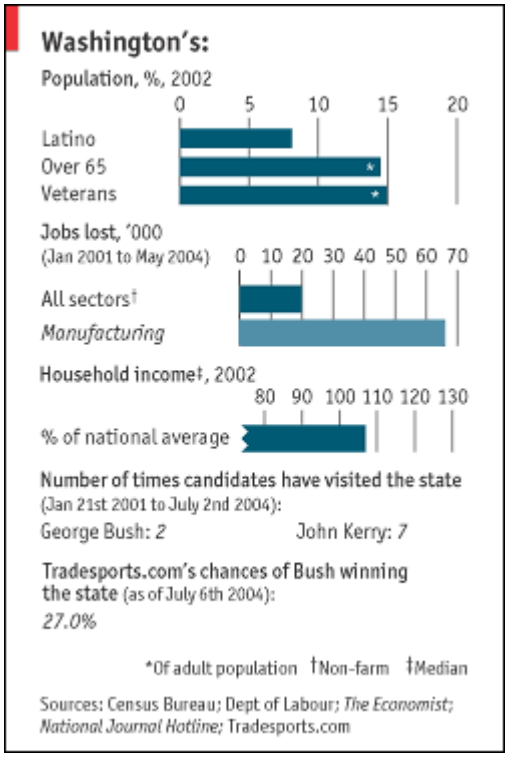
In the case of Seattle and voter-rich King County, that means being a northern version of San Francisco and the Bay Area. Patty Murray, a pro-choice “soccer mom” who is now running for her third term in the Senate, voted against the Iraq war and in 2002 contrasted Osama bin Laden's popular development projects in the Middle East with America's bombing campaigns. Jim McDermott, the congressman for Seattle, criticised the strikes on Afghanistan, went to Baghdad in September 2002, attacked Mr Bush for his willingness to “mislead the American people”, and was one of 11 Democrats refusing to vote in support of America's troops and president as the Iraq war began. Yet, for all that, his seat is rock-solid safe.

If the Democrats swing towards one extreme, the Republicans veer towards the other. In 1988, they chose as their presidential candidate not the incumbent vice-president, George Bush senior, but Pat Robertson, a right-wing televangelist with not a hope in heaven or hell of being elected. Four years ago they chose another

ultra-conservative, a talk-show host called John Carlson, to run against Gary Locke, the incumbent governor, and managed to lose not just west of the Cascades but to their east, too.

This time there are signs that Mr Vance has managed to restrain the state party, forcing it to choose moderates who just might appeal west of the Cascades. Dino Rossi, a former state senator with a record of firmness on law and order, is running to succeed Mr Locke (who has decided not to run for a third term); George Nethercutt, a congressman who won his seat in 1994 by beating the then speaker, Tom Foley, is running against Ms Murray for the Senate.

The Democrats profess to be unworried: they are ahead in the polls for both the Senate and the governorship. And they are adamant that Mr Bush is a hard sell in a state which has lost some 67,000 manufacturing jobs (many of them at Boeing) since he entered the White House. Unemployment in the Seattle region was under 3% in 2000; now it is double that level and worse than Anchorage's.



In principle, Mr Kerry is the sort of liberal Democrat who will go down well in King County, whose attacks on outsourcing will appeal to Washington's unions, and whose war record will impress the 15% of voters who are veterans. But there are plainly vulnerabilities for Mr Bush to exploit. Stuart Elway, an independent pollster, notes that after the Bush campaign used a batch of aggressive TV ads to greet Mr Kerry's effective nomination in March, Mr Bush was only five points behind Mr Kerry, compared with the 14-point gap with the "Democratic opponent" in January—though the president seems to have fallen further behind since then, even in Republican territory.

Another problem for Mr Kerry, in a state with no party registration, is that the electorate is an independent bunch. In 1994, they changed the congressional delegation to Washington from 8-1 Democrat to 7-2 Republican. In 2000, they turfed out Slade Gorton, a veteran Republican, and sent Maria Cantwell, a Clintonian New Democrat, to the Senate.

So there is hope for Mr Bush. But David Olson, a professor at the University of Washington, still thinks that the Republicans' main aim is to force Mr Kerry to spend money in the Pacific north-west. If he succeeds in that, Mr Bush will probably be very happy.

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The Cosby Show

Jul 8th 2004
From The Economist print edition

A comedian with a message that is worth listening to

BILL COSBY has had it up to here with black street culture. “Your dirty laundry gets out of school at 2.30pm every day, it's cursing and calling each other nigger,” he recently told a group of black leaders. “They think they're hip. They can't read; they can't write. They're laughing and giggling, and they're going nowhere.” The man who is arguably America's most admired black entertainer has turned from the long-suffering dad in “The Cosby Show” into a searing social critic. He dislikes entertainers who play to black stereotypes. He dislikes black street slang (“You can't be a doctor with that kind of crap coming out of your mouth”). And he dislikes parents who blanch at spending $200 on reading programmes but give their children $500 sneakers.

Good on Mr Cosby. There is something of a conspiracy of silence about blacks' dismal performance in school: silence from black leaders who don't want to be accused of “blaming the victim”, silence from teachers who don't want to draw attention to the biggest failure of American education. But the achievement gap between blacks and whites is a disgrace.

Black high-school students graduate an average of four years behind white students in basic academic skills. Most black students perform “below basic” in five of the seven key subjects measured by the National Assessment of Educational Progress. These dismal results are putting a ceiling on blacks' upward mobility—a ceiling that is getting ever lower as routine jobs are exported abroad or mechanised out of existence.

The teachers and black politicians blame three standard villains: poverty, prejudice and school funding. A third of black children are brought up in poverty compared with just 13% of white children. Seven in ten black children attend predominantly minority schools, up from 63% in 1980; more than a third attend schools with a minority enrolment of 90-100%. But these villains nevertheless leave a lot unexplained.

Take poverty. American history is full of examples of impoverished immigrants (Jews a century ago, Asians today) who have made it from the inner city to the Ivy League. More worrying still, the achievement gap is just as marked for affluent black children as it is for poorer ones. Or take school funding. There is no simple correlation between education spending and school quality. In “No Excuses: Closing the Racial Gap in Learning”, perhaps the best book on this subject, Abigail and Stephen Thernstrom point out that Cambridge, Massachusetts, was left with a huge gap between black and white students despite spending $17,000 for each and every pupil.

Or take prejudice. The percentage of people who tell pollsters that they have nothing in common with people of other races has declined from 25% in 1988 to just 13% in 2003. This is partly because the difference of income between blacks and whites with the same skills in maths and literacy has almost disappeared. Yet, over the same period, the gap in academic achievement has actually widened.

All this suggests that Mr Cosby is on the right track. Researchers routinely explain Asian children's success in terms of Asian cultural values. So why not admit that black children are failing because their culture undervalues success at school—because so many black children dream of becoming sports stars rather than professors, because bookish black children are stigmatised for “acting white”, and because almost half of black ten-year-olds spend five hours or more each day watching television?

Mr Cosby's diagnosis of black failure has another great merit. It comes with a remedy attached. Black America once had a flourishing tradition of self-help: the tradition of Frederick Douglass, who was born into slavery but became one of the great orators of his age, and of the army of self-educated blacks who came after him. This tradition was obscured during the civil-rights era as black leaders concentrated on dismantling the machinery of discrimination. But blacks desperately need to revive Douglass's belief in "self-cultivation" if the civil-rights revolution is to amount to something more than a hollow legal shell.

A broadside too narrow

Mr Cosby is well qualified to encourage this revival. He grew up in a poor area of Philadelphia and dropped out of school to join the navy. But he returned to university to take a doctorate in education, and continues to devote his energies to black improvement, writing books for pre-school readers and pouring money into black colleges.

He has drawn flak, of course. But the real problem with his broadside is that it is too narrow. It is not just black leaders who are failing to hold young blacks to higher standards. It is America in general—and, above all, the educational establishment. Teachers are far too willing to make excuses for black failure, and universities have institutionalised low expectations through affirmative action. Why should black children try as hard as their white peers if they can get into college with lower marks?

There are some signs that America is trying to tackle what George Bush once described as "the soft bigotry of low expectations". The Thernstroms produce plenty of examples of minority schools that are raising academic performance through discipline and accountability. The No Child Left Behind Act—perhaps Mr Bush's most underestimated achievement—is explicitly designed to close the racial achievement gap through a combination of testing and penalties for poor schools.

Changing the attitudes of young blacks will not be easy. It is always tempting to idolise celebrities who get paid millions of dollars while misbehaving. And it is always tempting to blame your problems on "society" when "society" has enslaved and disenfranchised your ancestors. But one thing is certain: black America's future will remain dim unless it begins to take Mr Cosby's jeremiads to heart.

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Venezuela's referendum campaign

Chávez's mission to get out the vote

Jul 8th 2004 | CARACAS
From The Economist print edition

AP

The president's social programmes may scoop up more votes for him in next month's recall referendum. It is less clear whether they help the poor

Get article background

FIVE years after Hugo Chávez, a former army officer, was sworn in as president promising a “peaceful revolution” to help them, Venezuela's poor are worse off in almost every measurable respect. Yet millions of them are likely to vote for him in a referendum on his presidency due on August 15th. Their support could save him: the latest polls suggest he might narrowly win the referendum. The recall campaign by the opposition Democratic Co-ordinator coalition is off to an unconvincing start. It needs at least 3.8m votes to revoke the president's mandate, but lacks both a message and a leader. Mr Chávez, on the other hand, is counting on a trump card: the “missions”.

“I hope Chávez rules for 100 years,” says Rosa Amarista, aged 73, as she finished a literacy class in a sprawling slum in western Caracas. “If he'd shown up 40 years ago I'd have a doctorate by now.” The class, in a community library, is part of the “Robinson Mission”, a literacy scheme which takes its name from a pseudonym adopted by Simón Rodríguez, a 19th-century educational pioneer and one of Mr Chávez's heroes. After two previous efforts to tackle illiteracy faltered, Fidel Castro, Cuba's president and a close ally of the president, stepped in to supply teaching materials and teachers. Robinson's popularity has led to a proliferation of new “missions”, especially for education and health care. These amount to a parallel social-service system, mostly funded outside the national budget.

They are popular. According to a survey in May by Datanálisis, a pollster, 57% of respondents approved of the Robinson Mission, even though fewer than 4% of Venezuelans are illiterate; Mr Chávez's own approval rating was only 43%. The other missions are equally approved of. They have become the centrepiece of the government's campaign. “The missions are ours—let's defend them,” is Mr Chávez's main slogan for the referendum.

That is a headache for the opposition. Tarek William Saab, a Chavista legislator, claims that all such social programmes will be swept away if the opposition comes to power. The opposition denies the claim, but is not widely believed. “All programmes will be evaluated,” according to Enrique Mendoza, the governor of Miranda state and the Co-ordinator's main leader. “Those with high social productivity and clear management will be retained. Those that...proselytise, manipulate and blackmail will disappear. For every programme that disappears, we'll be obliged to create two more.”

Part of the opposition's problem is that it is still associated with the discredited two-party system that Mr Chávez tore down. “For more than 40 years,” says Deomari Alvarado of the Ribas Mission for adult education, “governments did not concern themselves with educating the people as a whole—just a tiny elite.”

In fact, the statistics show a massive increase in schooling during the first two decades of the old regime after 1958. In the 1980s, oil income per head began to fall steeply. Corruption and mismanagement took hold. Now, for every 100 children who enter primary school, a mere 16 complete secondary education. But these figures have not improved a jot since Mr Chávez came to power. The Ribas Mission is for the 1.5m or so Venezuelans over 18 who never completed high school. So far, says Ms Alvarado, more than 700,000 have enrolled. Meanwhile, the normal school system is still marred by truancy, lack of funds and poor results.

In focusing on education and health, Mr Chávez has correctly identified some of the sources of Venezuela's big inequalities. But many poverty experts fault his solutions. Luis Pedro España, a sociologist at the Catholic University in Caracas, argues that the missions cost too much to sustain over a long period. And little attempt is made to disguise the missions' party-political motivation. Loyalty to what government supporters call “the process” (ie, Mr Chávez) is often demanded of participants. Announcing “Robinson”, the education minister's tongue was assumed to have slipped when he said the aim was to produce a million new *electores* (voters) instead of *lectores* (readers). But after he repeated the word three times, the message became clear.

Along streets and highways, Ribas Mission billboards promise a bright future. “Today, a maid. Tomorrow, a social worker,” says one poster, featuring a smiling young woman. But unemployment has jumped from around 12% to over 17% since Mr Chávez took office. Almost 80% of respondents in the Datanálisis poll are dissatisfied with the president's record on jobs. Another mission that is described as a job-creation programme is just a training scheme. One of the president's advisers says the idea is to create entrepreneurs, not jobs, since wage labour is “a form of slavery”. But the streets of Caracas are already clogged with “entrepreneurs” selling everything from hotdogs to pirated CDs.

The opposition claims that as the referendum approaches, the missions are being used to give government supporters preference in the provision of identity cards and in electoral registration. In the end, the result of the referendum may depend on whether it is truly free and fair. In a worrying sign that it may not be, the electoral authority this week proposed tight restrictions on foreign observers.

Whatever their social utility, the political importance of the missions is clear. To pay for them, Mr Chávez has adopted increasingly desperate measures. Earlier this year, he proposed to raid the Central Bank's reserves. Dissuaded, he has turned to Petróleos de Venezuela, the state oil monopoly, which is devoting 30% of its investment budget this year to social projects. It has set up a $2 billion social fund, into which it has already placed $750m in cash. Many of the company's offices are now being used for the same cause. “If the oil price fell to its average level in 2001, that would be enough to make the whole scheme fall apart,” points out Mr España. But well before it does, Mr Chávez doubtless hopes to have seen off his opponents.

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Presidents in trouble (1)

Bitten by Chihuahua and others

Jul 8th 2004 | MEXICO CITY
From The Economist print edition

Both Mexico and Peru have presidents who have become lame ducks long before the end of their terms

Get article background

HIS presidency still has two years left to run, but events this week showed that power is already slipping from the grasp of Vicente Fox. In elections in three states on July 4th, his conservative National Action Party (PAN) suffered a drubbing. Two were won by the resurgent Institutional Revolutionary Party (PRI), the main opposition. Worse, these states—Chihuahua and Durango—form part of what was once the PAN's northern heartland.

The next day brought even worse news for Mr Fox. His private secretary and chief spokesman, Alfonso Durazo, resigned. The ostensible cause of his departure could not have been better calculated to wound his ex-boss. In a long and detailed resignation letter, Mr Durazo picked on the presidential ambitions of Mr Fox's wife, Martha Sahagún, as his main reason for quitting.

AP

Two Foxes—but at what price?

If Mr Durazo's resignation came out of the blue, the poor election results had been widely anticipated. They were the first in a string of 13 state and local elections in the second half of this year. These should provide early clues as to which party will triumph in a presidential election in 2006. On current trends, it looks like the PRI, which governed Mexico for seven decades until Mr Fox's victory in 2000. Its success in Chihuahua and Durango echoed its strong showing in last year's mid-term congressional election. In the third state, Zacatecas, the left-wing Party of the Democratic Revolution retained the governorship, with the PAN a distant third.

Most dispiriting for the PAN was the loss in Chihuahua, not just of the governorship but of several big city mayoralties, including Ciudad Juárez, which it had governed for a dozen years. That comes on top of the loss last year of another northern stronghold, Nuevo León, whose capital is Monterrey, an industrial centre.

“A setback but not a disaster,” claims Juan Molinar, a PAN congressman. Apart from a weak candidate in Chihuahua and a low turn-out, he argues that the main reason why the PAN has been doing badly in the north is that this industrialised region bore the brunt of job losses in 2002-03, when the economic slowdown in the United States hit Mexico's *maquiladora* assembly plants. With the economy now recovering, some of those jobs may return before the 2006 election. PAN officials say that they will start panicking only if they lose elections next month in Baja California and Aguascalientes. Both are states where the party is strong.

One bright spot for the party was the victory of Andrés Bermúdez, the so-called “Tomato King”, who was elected as mayor of his home town, Jerez in Zacatecas. He runs a farming business in California, where he lives. He is one of the first migrant candidates to win elected office in Mexico—many more may follow.

Polls show that most Mexicans still like Mr Fox but have given up on his promises to “transform” their country. Faced with a hostile Congress, he has proved incapable of implementing policy change. In his letter, Mr Durazo described a presidency now largely in thrall to the political aspirations of Mrs Fox. He

drew a parallel with the PRI president, who used to handpick their successors.

He should know, shot back enraged PAN officials. They accuse Mr Durazo of betrayal, pointing out that before joining Mr Fox in 2000, he worked for the PRI. Mr Durazo may have done greater damage to the presidential couple than the state elections. He has written a new chapter in the soap opera of speculation over Mrs Fox's political ambitions, which already overshadows everything the president tries to do. And, fairly or not, by portraying Mr Fox as a henpecked husband he has added to his image of impotence.

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Troubled presidents (2)

Strikes, sleaze and violence

Jul 8th 2004 | LIMA
From The Economist print edition

How Alejandro Toledo became Latin America's least popular president

Get article background

IN SPAIN on a state visit this week, Alejandro Toledo warned of growing discontent in Latin America because of a “divorce between economic policies and the concrete results people see in their pockets.” Of all of the region's leaders, Mr Toledo has cause to know that. Since he took office in 2001, Peru's economy has grown at 4% a year or so. But he is the most unpopular president in Latin America, his approval rating in opinion polls below 10%. In those polls, more than half of respondents think he should go before the end of his term in 2006. Some Peruvians are now doing their best to make that happen.

AFP

Ayacucho, just where the Shining Path came from

Mr Toledo's political weakness is a factor in a wave of protests, some violent, that is shaking Peru. Doctors, pharmacists and airport workers are striking for more money. The largest labour federation has called a one-day general strike on July 14th, in protest at the government's economic policies. The strike is supported by APRA, the main opposition party.

Last week, in Ayacucho, a city in the poor Andean interior, striking teachers and their supporters fought police for ten hours, setting fire to several public buildings including the local offices of the judiciary, where thousands of files of drug-trafficking and terrorism cases were destroyed. Ayacucho was the birthplace of the Maoist Shining Path guerrillas, and it also produces much coca (from which cocaine is made). The government blames Shining Path supporters for the violence. But the regional president said that Mr Toledo's ineptitude has allowed lawlessness to take root. In April, a mayor in a town near the Bolivian border was lynched; other small-town mayors in the Andes fear the same fate.

Mr Toledo and his government's economic policies have survived previous waves of protest more or less unscathed. Will this time be different? Officials hope that Peruvians will pay less attention to the general strike than to the Copa America, the South American football championship, which kicked off in Lima on July 6th. The disorder is isolated and sporadic, reflecting local problems, rather than a sustained campaign.

But Mr Toledo's troubles are deepening. His party has shed congressmen, losing two in as many weeks. It now has only 38 seats in the 120-seat Congress and is likely to lose the presidency of the legislature this month. The president also faces mounting allegations of corruption. In a recent poll, more than 70% of respondents said Mr Toledo—who campaigned against the sleaze of Alberto Fujimori, the authoritarian

president of the 1990s—was himself corrupt. In addition, a claim has emerged that his party forged the signatures it collected to register his candidacy for an election in 2000.

Should more evidence emerge to support all these claims, talk of impeaching the president is likely to follow. But do the politicians want to do that? Apart from Mr Fujimori's supporters, nearly all of them desperately want Peru's restored democracy to succeed. The campaign for the 2006 election will start early next year. If Mr Toledo survives until then, he is probably safe. But testing months lie ahead.

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Polygamy in Canada

Hunting Bountiful

Jul 8th 2004 | VANCOUVER
From The Economist print edition

Ending half a century of exploitation

THEY like to think they do a good job protecting women's rights and fighting paedophilia. Canadians would not be so smug if they knew of the dirty little secret in the Creston Valley, in south-eastern British Columbia. For half a century, a hotbed of polygamy has quietly flourished there in a commune called Bountiful. It is run by a breakaway sect of the Mormon Church, in successful defiance of the law.

Bountiful is no secret to local people, some of whom enjoy its business. Nor is it to the province's police and social workers. It is known to British Columbia's top law-enforcement officer, the attorney-general. His office was first made aware of concerns about Bountiful more than a decade ago. But the provincial government has felt constrained by an untested legal opinion that Canada's law banning polygamy was unconstitutional.

Bountiful claims allegiance to the Fundamentalist Church of Jesus Christ of Latter-Day Saints. Based in Utah, this dissenting Mormon sect teaches that men must have three or more wives and as many children as possible to enter heaven. The role of women and girls is to serve men. If women disobey men, their souls will burn in hell for eternity.

The commune was quietly set up in 1947, after a few men excommunicated by the mainstream Mormon Church in Utah (which banned polygamy in 1890) moved north. Today the 1,000-odd residents are almost all the progeny of half-a-dozen men. The place is dominated by the “bishop”, James Oler, and by his deposed predecessor, Winston Blackmore, who now heads a splinter group.

Both groups run schools. These receive grants from the provincial government totalling more than C$600,000 ($450,000) a year. Yet critics say they provide minimal education, preparing boys only to work on Bountiful's farms and forests and girls to be “young brides and mothers”. Women who have fled tell of girls as young as 13 being married off to polygamous men three times their age; of babies born to girls of 14 and 15; and of under-age girls being brought in from similar American communes for arranged marriages and to serve as “breeding stock”.

“A grotesque and blatant infringement of human rights,” says Jancis Andrews, a women's-rights advocate. Geoff Plant, the attorney-general has plainly been embarrassed by years of criticism of his inaction. His inertia stems from a case in 1992 when police recommended that two Bountiful men be charged with polygamy. But the crown attorney's office declined to do so, following legal advice that conviction was impossible because the guarantee of religious freedom in Canada's Charter of Rights and Freedoms renders the law against polygamy unconstitutional.

That opinion is disputed. The federal justice ministry believes the law to be constitutionally sound, and has offered to throw its weight behind any prosecution. Now it may have a chance to do so. In May, nine women fugitives from Bountiful filed a complaint with Mr Plant's office alleging polygamy and sexual abuse of girls as young as 13. Mr Plant says that he has “indicated” to the police that “the existence of a constitutional opinion on the enforceability of [the law on polygamy] is not a reason for the entire public criminal-justice system to sit on its hands.” The police are now at work. The hunters of Bountiful's dubious practices are closing in.

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Indonesia's presidential election

Now, at last, the voters are in charge

Jul 8th 2004 | JAKARTA
From The Economist print edition

AP

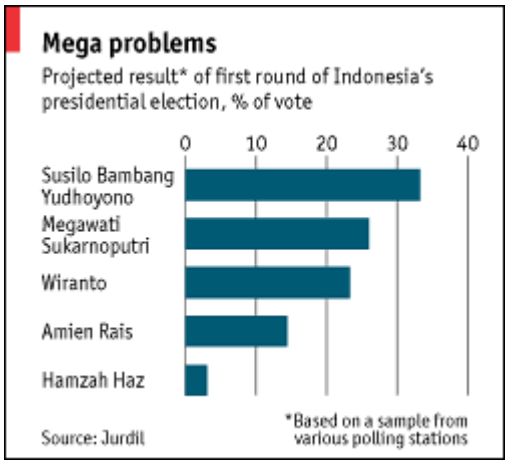
No outright winner yet, except perhaps democracy itself

Get article background

FROM the early morning, voters queued up diligently to collect their ballots, punch a hole in the picture of the presidential candidate of their choice and drop the paper in the box. An ordinary election in many countries—but an extraordinary one in Indonesia. Even after the overthrow in 1998 of Suharto, the country's strongman for three decades, and despite the restoration of democratic elections to parliament the following year, Indonesian legislators continued to elect (and depose) presidents without a popular vote. So July 5th marked the culmination of the country's tumultuous transition to democracy.

In fact, the transition will drag on a little longer, until a run-off vote on September 20th, since none of the five candidates appears to have won an outright majority in the first round. It may take as long as three weeks to compile the final results, but as the polls had predicted, Susilo Bambang Yudhoyono, a former general (pictured above), is leading the race. When *The Economist* went to press, he had won 34% of the vote, with over half the ballots counted. Behind him, in a close contest for the remaining slot in the run-off, were Megawati Sukarnoputri, the incumbent, with 26% and Wiranto, another former general, with 22%. The final result should be similar, according to Jurdil, a consortium of NGOs that conducted a sample of actual returns from polling stations around the country (see chart).

Some doubt remains, however, thanks to a Florida-style fiasco during the counting. Voters were supposed to punch just a single hole in the ballot. But many did not bother to unfold the concertina-like paper completely before making their choice, and so perforated the ballot several times. As counting began, the election commission ordered poll workers to accept these spoiled ballots, as long as the extra holes fell only in blank spaces. But many polling stations did not receive these instructions in time, if at all, while others refused to take on the extra work.



At the polling stations surveyed by Jurdil, about 9% of ballots were originally set aside as spoiled, although in some districts the share was much higher. Poll workers would subsequently have recounted many of those, leaving the final proportion of spoiled ballots similar to or less than the 7.5% recorded in legislative

elections in April. Anecdotal evidence from the recounts suggests that the debacle has not done any particular candidate down. But witnesses for the candidates did not monitor many of the recounts, and poll workers applied the commission's revised rules inconsistently. The number of votes involved will almost certainly exceed the margin between the second- and third-placed candidates. So a disgruntled number three—in all likelihood, Mr Wiranto, but still, just possibly, Miss Megawati herself—could easily find plausible grounds to reject the results.

Whichever candidate Mr Susilo faces, he goes into the second round the favourite. Pollsters say he is popular all over Indonesia, with both young and old, rich and poor, men and women, and city and country folk. Critically for the run-off, he was the second choice of most Indonesians who did not intend to vote for him in the first round, according to several pre-election polls and focus groups. A study conducted by the International Foundation for Election Systems (IFES) found that only 2% of Indonesians have a negative opinion of him, compared with 20% for Miss Megawati and 9% for Mr Wiranto. Exit polls suggest he attracted support not only from members of his own, relatively small party, the Democrats, but also from Golkar, Mr Wiranto's party, and several Islamically-inclined parties.

Miss Megawati's vote, on the other hand, derives mainly from members of her own secular nationalist party, PDI-P. But PDI-P is much bigger and richer than the Democrats, and Miss Megawati's vote held up better than many imagined. She will be able to use all the benefits of incumbency to promote her candidacy over the next two and a half months. Endorsements and alliances could also help tip the scales. For example, the endorsements of the National Awakening and Prosperous Justice parties, neither of which fielded a candidate in the last round, will be up for grabs again.

In other words, anything could still happen. Indonesian voters, who were often assumed to follow primordial loyalties of ethnicity and religious outlook, are proving to be surprisingly independent-minded. After all, two brand-new parties, the Democrats and Prosperous Justice, together polled almost 15% of the vote in April's legislative election. In this week's poll, supporters of the Nahdlatul Ulama and Muhammadiyah, Indonesia's two biggest Muslim organisations, plumped for many different candidates of varying degrees of piety. Provinces that had been squarely in Golkar's camp in April's election swung to Mr Susilo. The front-runner himself barely registered in opinion polls as recently as February.

But Indonesian voters are also level-headed and responsible. Some 80% of registered voters, or roughly 125m people, turned out. Even in the country's many restive regions, there was little violence during the campaign or on polling day. None of the candidates is a populist or firebrand, and Mr Susilo and Miss Megawati, in particular, both espouse sensible, moderate, secular views. Cheered by all this good news, Jakarta's stockmarket rose by 3% the day after the vote, and the rupiah climbed to its highest value against the dollar since early May. According to IFES's pre-election poll, no less than 84% of Indonesians thought the election would be fair. That, surely, is the best result of all.

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Cambodia

Inveterate suspicions

Jul 8th 2004 | PHNOM PENH
From The Economist print edition

Cambodia's long-awaited new government is not off to an ideal start

NOTHING is ever easy in Cambodia. A year after its general election, Hun Sen, the leader of the Cambodian People's Party (CPP), and Prince Ranariddh, the leader of the royalist FUNCINPEC, finally signed an agreement last week to share power, with the former as prime minister and the latter as speaker of the National Assembly. But almost immediately, there was a snag.

The constitution calls for the speaker to be elected before the prime minister, and Mr Hun Sen, apparently, fears that Prince Ranariddh, once installed in the speaker's chair, will renege on the deal and refuse to confirm him as prime minister. So when the Assembly convened on July 8th, he insisted that its first act should be to amend the constitution, to allow the speaker and prime minister to be elected simultaneously.

Such inveterate suspicion has helped to prolong the year-long stand-off among Cambodia's feuding politicians. The row began thanks to another clause in the constitution, stating that a new government requires the support of two-thirds of the members of the National Assembly. The CPP, which led the previous government, fell just short of the threshold in elections last July. But it had great trouble persuading either of the other two parties in the Assembly to join it in government. Instead, FUNCINPEC and the reformist Sam Rainsy Party (SRP) formed an “Alliance of Democrats” dedicated, ironically enough, to scuppering any new government until the CPP made various concessions.

Mr Hun Sen, in turn, rejected the idea of a three-way coalition. But recently, the three parties agreed on a face-saving formula for a “two-and-a-half-party” coalition, whereby the CPP and FUNCINPEC will form a government on their own, but FUNCINPEC will nominate SRP members to some of its ministerial posts. A 73-point legislative programme was also squared away. The final bone of contention was the allocation of ministries, with the two sides finally accepting a 60-40 split, in line with election results.

The dispute dragged on so long because coalition negotiations are about the only leverage the other parties have over the CPP. It used to rule the country as a one-party state, and still dominates the bureaucracy. FUNCINPEC ministers in previous governments say that civil servants simply ignored their instructions. The SRP, meanwhile, accuses the CPP of exploiting its authority to rig elections and repress dissent.

The new arrangements are unlikely to change any of that. For all its bluster of the past year, FUNCINPEC seems no more willing to stand up to the CPP than during the parties' two previous coalition governments. In other words, it has taken Cambodia a year to get back to where it started.

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Asian security

Regionally challenged

Jul 8th 2004
From The Economist print edition

Let a hundred forums bloom

WHEN America's secretary of state, Colin Powell, dressed as a construction worker, belted out his rendition of “YMCA”, at the closing dinner last weekend of the Association of South-East Asian Nations' (ASEAN's) Regional Forum (just call it the ARF) in Jakarta, he was not trying to add to the acronym soup that now drenches this annual ASEAN event. (Aficionados can enumerate a long list of such ASEAN offshoots, starting with AFTA, its free-trade area.) Rather he was hoping to top the legendary performance by America's Madeleine Albright and Russia's Yevgeny Primakov, who joined diplomatic gangs at this event six years ago for a hugely successful post-cold-war excerpt from “West Side Story”.

The ARF's reputation as the place where foreign ministers and other senior people from Asia, Europe and North America meet and make merry may not last. In 2006, military-ruled Myanmar will be in the chair. America has already said that, unless Myanmar is by then well on the road to democracy, there will be no visit from its secretary of state. The European Union is similarly threatening to stay away from an Asia-Europe (ASEM) summit in Hanoi in October.

However, the bigger threat to diplomatic co-operation in Asia may come from the proliferation of talking shops, not the problems of the ARF. In the post-September 11th world, everyone is in on the act. Even APEC, short for Asia-Pacific Economic Co-operation (once described memorably if loosely as four adjectives in search of a noun), which brings together the two sides of the Pacific, issues statements on terrorism and the like.

Still, the ARF is supposed to be the place where more than declaratory work on security is done. This year's summit was organised to allow more time for behind-the-scenes diplomacy: North Korea's foreign minister was in attendance, and met both Mr Powell and others involved in the six-way talks on the North's nuclear programmes. That particular issue is too sensitive, involving bigger fry, such as America, China, Russia, Japan and South Korea, for the less powerful countries of South-East Asia to play much of a role. For precisely that reason, there is hope among some of the six of continuing the six-way format (though presumably not always with the prickly North Koreans along) as a place where harder issues can be discussed.

Adam Ward, of the International Institute for Strategic Studies (IISS), a think-tank in London, says that ASEAN itself is too obsessed with managing China to give much thought to wider concerns. Yet the relationship, he argues, is really working the other way. At China's initiative, ASEAN has given the go-ahead for the launch of a new Security Community (adding the ASC to the acronym bowl) among its members to discuss issues such as maritime safety and intelligence exchanges. For China the ASC offers a useful rival to other less formal security dialogues, including an annual meeting for defence ministers run by the IISS, that it finds harder to control. The ASC will be easier for China to bend to its foreign-policy aims, which include the blocking of all discussion of that other East Asian security hot potato: its own stand-off with Taiwan.

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India's budget

High-wire act

Jul 8th 2004 | DELHI
From The Economist print edition

The new government's first budget is balanced but hardly inspiring

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FOR Palaniappan Chidambaram, the finance minister in India's new ruling coalition, his first budget speech, delivered on July 8th, required tightrope-walking skills of a high order. The coalition is not only an untidy collection of parties, including those that represent India's poorest, but also depends on the country's communists for parliamentary support. In order to placate these powerful partners, Mr Chidambaram produced a budget that may not have upset anyone, but that has done little to advance reform.

Keener reformers wanted to see immediate action on privatisation, the slashing of India's labyrinth of subsidies and the radical reform of labour laws. They got none of this, even though some other significant reforms, especially in the area of deregulation, are to go ahead. The new finance minister has also promised to shrink a government deficit that absorbs far too much of India's resources. And he has managed to sidestep many of the costly proposals in the coalition's Common Minimum Programme (CMP) by passing them on to India's planning commission for assessment.

Mr Chidambaram made his speech against the background of the government's annual economic review, published on July 7th, which estimated annual economic growth of 8.1% for 2003-04 and set a 7% to 8% target for the next five years. The 8.1% is somewhat less impressive than it looks, because it marked a recovery from a mere 3.7% in 2002-03 when one of the worst droughts for decades pushed agriculture to negative growth of 5.2%.

Agriculture accounts for the livelihood of 70% of India's population. It is also a focal point of the CMP, reflecting the fact that the coalition's unexpected victory in May's general election was owed mainly to dissatisfaction with the economic and social policies of the former Bharatiya Janata Party-led central government and several state governments.

Accordingly, agriculture and rural areas were a central focus of Mr Chidambaram's speech. He is offering a range of support and incentives, including a doubling of agricultural credit over three years, widespread water schemes, and help for diversification into new farm products and food processing. This echoed the themes of a speech on June 24th by Manmohan Singh, the prime minister, who promised “a change in the manner in which this country is run” and said that economic growth should “advance the cause of distributive justice and recreate new employment opportunities”. Politically astute, no doubt, but possibly not the stuff of which a new Asian tiger is made.

The macroeconomic framework, however, is favourable. Though he seemed loth to credit the previous BJP government with any success, Mr Chidambaram has inherited a substantially improved fiscal deficit which (including both central and state governments) has been brought down from 10.1% of GDP in 2002-03 to around 9%. The central-government deficit is down for 2003-04 from 5.3% to 4.6% and the states' deficit is expected to come down from 4.7% to around 4.2%—partly due to improved growth and an increased tax take. Foreign-exchange reserves are also strong, having reached a record of $119 billion at the end of May. Wholesale-price inflation is running at about 5%.

On industry, Mr Chidambaram balanced the wishes of reformers and the leftist parties by announcing a new commission to boost both foreign and domestic investment. “The key to growth is investment,” he said. “Public and private, domestic and foreign.” So he raised the limits for foreign ownership in two areas where joint-ventures urgently need fresh funds from abroad—insurance (from 26% to 49%) and telecoms (from 49% to 74%). He also raised the limit for civil aviation from 40% to 49%. These increases should help to boost India's poor record on investment inflows, which fell in 2003-04 from $4.7 billion to $4.5 billion (a tiny fraction of what China takes). Limits, though, are only part of it: foreign investment is mostly restricted by foreign companies' frustrations with India's bureaucracy and poor public services and infrastructure.

Reformers will, however, be less than delighted with his pro-leftist attempt to rebuild India's public sector instead of trying to privatise it. He announced the creation of a Board for Reconstruction of Public-Sector Enterprises that will advise on how to develop (and with luck occasionally sell) government-owned companies; and he pledged government funds for major investments in public-sector power, telecoms, railways, roads, petroleum, coal and civil aviation.

Some of this will be paid for by a limited programme of privatisation: one power utility, for instance, is about to raise funds through an issue of shares that will dilute the government holding, though only by 5%. Yet Mr Chidambaram failed to explain how the government plans to make its investments in the public sector any more effective than before. This is not the end of reform in India, nor is it an inspiring start for the new government's efforts to advance it.

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Afghanistan

Where foresters fear to tread

Jul 8th 2004 | AJAR VALLEY, WESTERN HINDU KUSH
From The Economist print edition

A fragile environment is under attack

“NOW is the time for conservation in Afghanistan,” says the country's former king, Mohammed Zahir Shah. The few environmentalists working in Afghanistan agree. Since the monarchy was overthrown in 1973, two decades of war and another of drought have ravaged what was already a marginal agricultural land. The dust storms that howl through Kabul during the summer were less common when the king ruled. In those days, the Shomali plain north of the city was thick with poplar, tamarisk, willow, hawthorn, walnut and apricot trees.

As in Bosnia, the rise of a machinegun culture has caused the slaughter of wild animals. *Mujahideen* guerrillas driven high on to the Hindu Kush by Soviet invaders gunned down leopards, steppe eagles, Siberian ibex, markhor and other endangered species. No one knows what is left. Afghanistan has hardly a single wildlife expert; its records were mostly burned during the war. National parks exist on the map but not in reality. The chief of parks shares a dingy office in Kabul with the heads of forestry and mountain pastureland. None of them has a car or a phone.

Deforestation is easier to track. Satellite imagery collected by the United Nations Environmental Programme (UNEP) suggests that the government of Hamid Karzai has done an even poorer job than the previous Taliban regime of protecting the thousand-year-old oak, pine and cedar forests in the ethnically Pushtun south-east. By official estimates, forest cover is down by 40% since the 1970s; locals put the loss closer to 60%.

An American idea to create an Afghan “Conservation Corps” would be next to useless in the Pushtun areas that most need it, given that not even American special forces can feel safe there. Senior officials enrich themselves by illegally felling forests—especially those of high-grade deodar cedars. The timber is trucked to Pakistan, where some of it is re-exported out of Karachi.

These eastern forests are where Osama bin Laden may be hiding. The tracks being cut through the trees by logging lorries might make it a bit easier to spot al-Qaeda fighters, but at a terrible cost. UNEP and Save the Afghan Environment, a local green group, reckon that villagers in deforested areas will suffer the same landslides and flooding that have devastated parts of rural Nepal—where poverty has made villagers more sympathetic to Maoist insurgents. In Afghanistan, the forests are being chopped down in areas where the government is already unpopular.

What can be done? Mr Karzai could start by reining in his log-thieving subordinates, with help from the NATO peacekeepers based in Kabul. He must act quickly. The country's former king says that much has already been lost, including most of the country's pistachio forests. To align conservation interests with those of locals would require training a new generation of foresters and conservation experts. Yet there are some filaments of hope. The ex-king's hunting reserve, in the Ajar valley, in the western Hindu Kush, may see some rudimentary training next year. And New Zealand, whose soldiers patrol a few hours south of the valley, in Bamiyan, is considering protecting Ajar as a proxy national park of its own.

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Australia

An island murder mystery

Jul 8th 2004 | NORFOLK ISLAND
From The Economist print edition

An unsolved killing causes tension between Australia and its island territory

NORFOLK ISLAND has always been a place of refuge. About half its 2,000 people are related to the *Bounty* mutineers, whose descendants moved there from Pitcairn Island in 1856. Other settlers came seeking a quiet life in one of the South Pacific's few tax havens. Lately, though, Norfolk Island has endured what some islanders consider its most terrible trauma since the dark days of the early 19th century, when it was a repository for British convicts.

Last month, a coroner reported on the death of Janelle Patton, a 29-year-old Australian resident whose body was found dumped on the island's north coast in March 2002. She had been stabbed and beaten to death. It was the first known murder in the island's history. The coroner recorded an open verdict, but sent shockwaves through Norfolk Island's tight-knit community by naming 16 “persons of interest” in the case. An Australian politician, Ross Lightfoot, stirred more anxiety by claiming that police efforts were being frustrated by a “husk of silence that surrounds Norfolk Islanders when they want to protect their own.”

Many islanders were already smarting over an earlier report by a parliamentary committee on which Mr Lightfoot serves that called for an end to Norfolk Island's self-governing powers over immigration and revenue-raising (it has no income tax). An Australian territory, set 1,000 miles (1,600km) from the the mainland, Norfolk Island has long had uneasy relations with Canberra. Residents call it a “distinct and separate settlement”, as Queen Victoria once described it. But the nosy parkers in Canberra seem to have seized on Ms Patton's murder as an excuse to intervene.

Colleen McCullough, an Australian novelist who lives on the island, is fiercely critical of her country's policies towards her adopted home. “Canberra is a child pulling the wings off the world's last specimen of a particular butterfly,” she says. Her husband, Ric Robinson, a descendant of the immigrants from Pitcairn Island, and John Christian, a descendant of Fletcher Christian, the mutineers' leader, are among a group campaigning for self-determination. Mr Robinson argues that oil and gas deposits in Norfolk Island's territorial waters could underwrite its independence.

Other nationalists fear independence could make the island a money-laundering hub; they want to retain a loosened link to Australia. Canberra may have to steer carefully to avoid another mutiny.

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Iraq

Who are the insurgents—and can they be defeated?

Jul 8th 2004 | FALLUJAH
From The Economist print edition

AFP

As the insurgents fight on, the new government hopes to divide and beat them

Get article background

TRYING to make good on his robust start in office, Iraq's new prime minister, Iyad Allawi, this week announced a new security law to give his fledgling security forces, aided by the American-led multinational force, wider powers to clobber the insurgents and their suspected helpers. Under a new "national safety law", his government can impose curfews, allow searches and detain suspects for up to 60 days. Mr Allawi's hope is that ordinary Iraqis, desperate for security, will turn against the insurgents, especially foreign ones, and deprive them of succour. It is too soon to see signs of this happening already. But divisions among the insurgents may be emerging for Mr Allawi to exploit.

The insurgency is still going strong. The shaky truce between the Americans and the rebels that has prevailed in their Fallujah stronghold, to the west of Baghdad, has enabled them to divert their energies elsewhere in the Sunni triangle west, east and north of Baghdad. This week insurgents battled with American and Iraqi troops in the heart of Baghdad. Masked men took control of Samarra, north of the capital, after American commanders pulled the last of their troops out of the town—and promptly banned the wearing of jeans. Insurgents claimed to hold another town, Qaim, on the Syrian border. Last week, wearing *jihadi* bandannas, they briefly occupied the centre of Baquba, north-east of Baghdad.

The new government stresses two factors that it hopes will work against the rebels. The first is the growing revulsion of many Iraqis towards the rebels' penchant for targeting all compatriots who are alleged to "collaborate" with the new regime and its foreign backers. This week, for instance, restaurants in Baghdad's poshest district, Mansour, shut down in protest against the killing of three waiters at one of Baghdad's best eateries, apparently for serving American troops. A barber in the same area was killed for similar reasons.

The second factor is the rebels' links with foreign *jihadis*, seen by many Iraqis as prolonging the country's agony for a dubious cause. This week the new justice minister, Malik Dohan al-Hassan, waved a list of 25 non-Iraqi names, blaming Syria and Iran, among others, for egging on outsiders to keep Iraq on the boil. A couple of days earlier, two Iranians were said to have been caught wiring up a car-bomb.

The degree of foreign involvement in Iraq's insurgency is uncertain. The interior ministry says that infiltrators have come from as far afield as Morocco and Chechnya. Some 8,000 volunteers came through Jordan and Syria to defend Iraq before the Americans attacked in March last year, but it is unclear how many stayed behind after Saddam Hussein was toppled.

What is clear is that many more *jihadis* did pour in after the conventional phase of the war. One early decree of the (now departed) American proconsul, Paul Bremer, abolished Iraq's border guard. Even today, only three of 36 former checkpoints on the long and porous border with Saudi Arabia are manned. Adnan Karim, a former admiral whose think-tank now analyses the rebel groups for Mr Allawi, reckons that Fallujah alone has 1,000 foreign *jihadis*.

Plainly, estimating the numbers is tricky. The justice minister admits that only 29 out of several thousand detainees suspected of rebel activity are foreign Arabs. American defence officials say that of 6,000-odd detainees held under their regime, some 90 were foreigners, of whom about half were Syrian. Judging by their accents on *jihadi* videos recorded before they go to their deaths, almost all the suicide-bombers in Iraq have been foreign.

But the biggest pool of rebels was almost certainly provided by Mr Bremer's dissolution of the 3m-strong Baath party and the 700,000-strong army and security forces. The Republican Guard, at the heart of Mr Hussein's forces, melted away during the war only to regroup after the conventional phase was over. The mainly Sunni officer class provide cash, training and arms for the rank-and-file.

With an eye to such people, Mr Allawi is offering an amnesty to “resistance fighters” provided they hand in their weapons. At the same time, he is trying to call back some six army divisions, totalling more than 50,000 men, who served under Mr Hussein. Once again, it is too soon to say whether such plans will bear fruit.

It is clear, in any event, that a portion of Iraqi rebels who started off as disgruntled demobilised soldiers have been converted to the Islamist cause. Mr Karim, Mr Allawi's admiral-turned-analyst, counts some 36 different Sunni insurgent groups, inspired by the beliefs of puritanical Salafis, Sufi mystics and Muslim Brothers. Others owe allegiance to tribal sheikhs. There is a powerful crew of *jihadi* Kurds. A further half-dozen Shia rebel groups, the largest led by an angry young cleric, Muqtada al-Sadr, operate in Baghdad and the south, says Mr Karim. It is not yet clear whether Mr Allawi will succeed in bringing the turbulent Mr Sadr peacefully on side.

The Salafis are the most dedicated, a shade more so than the Sufis. Originally a Saudi movement, their Iraqi branch dates back to the 1960s but stayed on the fringe for decades. Only in the 1990s, when the UN's economic sanctions made many Iraqis poor, bitter and prey to outside influence and cash, especially from Saudi Arabia, did the movement spread. After Mr Hussein's fall, its fundamentalist preachers seized the capital's biggest mosques and filled them with their followers.

“Iraqis who collaborate with Americans are apostates,” says their Baghdad mullah, Mehdi Sumeidi, using a term which in Islam carries a death penalty. Policemen who fight alongside unbelievers are unbelievers too, says another prominent Salafi, a dentist called Fakhri al-Qaissi, when asked about the killing of seven national guardsmen near Baghdad shortly after Mr Allawi took office. Mr Karim says that a Salafi jurists' council issues such *fatwas* for the rebels to implement.

Mr Fakhri says it has yet to be decided whether Mr Allawi himself is an infidel. But there is no doubt that the *jihadis*, who vaunt their record of fighting against western-backed dictators elsewhere in the Arab world, think they will gain strength as a result of Mr Allawi's much-heralded martial laws. Within hours of his declaration of them, missiles were fired at his party headquarters in Baghdad, rebels skirmished with nearby American forces, and a suicide-bomber blew himself up at a memorial service near Baquba attended by officials of the new government.

Nationalists versus the new caliphate

An early straw of hope for Mr Allawi is reported discord in *jihadi* ranks between Iraqi nationalists and the more zealous internationalists, apparently led by Abu Musab Zarqawi, a Jordanian with a reputation for damning colleagues with whom he disagrees as infidels. Even Osama bin Laden is said to have found him too extreme when they were together in Afghanistan.

A growing number of Iraqi insurgents are fed up with the car-bombings apparently organised by Mr Zarqawi's group and often set off by foreign *jihadis*. Iraq's Salafi preachers say that the rebels have no need of foreign help.

It may not be clear for a month or so whether Mr Allawi's efforts to divide the rebels, offer some of them an amnesty and tar their leaders with the brush of friendship with the likes of Mr Zarqawi have begun to

work. Meanwhile, he and his new team are bracing themselves for more violence, some of it aimed at themselves, as infidels and American puppets.

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Weapons of mass destruction

If you push, I'll shove

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Nuclear temptation in the Middle East

IF THE world is in for a dangerous nuclear chain reaction, its trigger could be in the already fissile Middle East. Arab governments point their finger at Israel, which has long been thought to possess up to 200 nuclear bombs. Israel, like India and Pakistan, has never signed the Nuclear Non-Proliferation Treaty (NPT). But it points the finger right back, at the chemical- and possibly biological-tipped missiles bristling in its neighbours' armouries.

This balance of insecurity was always uneasy. Now Israel's nuclear edge, which helped steady it, may be eroding. Of the four covert nuclear programmes discovered in recent years, three—Iraq's, Iran's and Libya's—are in the Middle East; the fourth is North Korea's. And there are suspicions that these may not be the last.

This week Mohamed ElBaradei, head of the International Atomic Energy Agency (IAEA), the UN's nuclear watchdog, was in Israel, partly for technical discussions (being outside the NPT, Israel's military sites, including its plutonium-producing reactor at Dimona in the Negev desert, are off-limits to inspectors but some civilian sites come under their safeguards), but also to suggest one answer to the accumulating nuclear threats: hold talks on a nuclear-weapons-free zone in the Middle East—before it is too late.

In the past, Israel has been ready to contemplate such a zone, so long as it included all weapons of mass destruction in the region, but only when there was a durable peace. Mr ElBaradei wants to encourage the idea that security talks should run in parallel to the fitful diplomacy in the region. Some Israelis are interested. But for the government, the opportunities have so far been outweighed by the threats.

Certainly, Saddam Hussein's hostile regime in Iraq, which fired missiles at Israel during the first Gulf war and whose own nuclear reactor at Osirak was bombed by the Israeli air force in 1981, is gone. Libya's decision last December to get out of the business of weapons of mass destruction took another country off Israel's threat list.

The information Libya handed over about its suppliers helped expose a vast global black market in uranium enrichment and other militarily useful skills centred on a Pakistani scientist, Abdul Qadeer Khan. Since Iran tapped into the same illicit network, all this helped the IAEA expose its 18 years of nuclear-safeguards violations: illegal nuclear experiments set out in a series of reports for all to see. Yet, troublingly, Iran shows no sign yet of giving up the dangerous technologies it has developed, despite a deal with Britain, France and Germany last year that they hoped would give it an opportunity and incentive to do so.

There is also the “fourth customer” problem. Although Mr Khan had admitted to selling his nuclear wares only to Iran, Libya and North Korea (all wilful breakers of NPT rules), there are suspicions that others may have availed themselves of his services. Although all supposedly bound by their non-nuclear promise under the NPT, few Arab governments have accepted the more intrusive safeguards and inspection regime devised after it was found how close Iraq had come to a bomb before the first Gulf war, without anyone knowing.

Who else, then?

Saudi Arabia has no safeguards agreement with the IAEA at all, though under the NPT it should. It has plenty of cash to buy in nuclear expertise. Back in the late 1980s it acquired Chinese-built CSS-2 missiles capable of striking anywhere in the region, and indeed beyond, with a nuclear or chemical warhead.

Having helped, it is said, to finance both Libya's and Pakistan's nuclear-weapons pursuits, some think it may have bought itself an option on a Pakistani bomb or two, should need arise.

Syria, which already has chemical and biological weapons, is a worry too. Unconfirmed reports suggest it may now have a covert uranium enrichment capability. And its efforts to acquire a nuclear desalination plant raise fears that it could some day acquire plutonium.

If Iran's Shia theocracy were to get its hands on a bomb, it is not only Israel that might be alarmed. Egypt has potentially militarily useful nuclear skills and an increasingly sophisticated missile programme. Algeria has a suspiciously large nuclear reactor in the Sahara, surrounded by missile defences. And there are fears that even Turkey, a NATO member, could reconsider its non-nuclear pledge, should others in the region seem about to renege on theirs.

Much depends on whether Iran's nuclear ambitions can be checked before it has a bomb. Some are urging Israel to help the diplomacy along, by declaring an end to its plutonium production and shutting down Dimona (where there are already safety concerns due to the reactor's age), by ratifying the Comprehensive Test-Ban Treaty (which it has already signed) and by taking other confidence-building steps.

But without a better outlook for stability in the region, let alone peace, Israel may prefer self-reliance. Its nuclear weapons can be carried on missiles and aircraft and perhaps now also on submarines armed with American-built Harpoon missiles modified to carry nuclear warheads. It has also hinted that if Russia shows signs of delivering fuel for Iran's nearly completed nuclear reactor at Bushehr, it would consider the sort of conventional strikes that knocked out Iraq's Osirak reactor. One way or another, the finger-pointing could yet turn deadly.

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Arabs and the internet

Watch out

Jul 8th 2004 | CAIRO
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The internet can undermine harsh regimes—and land its users in jail

ABDEL RAHMAN SHAGURI'S computer is an ordinary one, but when he clicked the “send” button on its e-mail programme back in February 2003 it sent him straight to jail. The 32-year-old from Damascus looks set to stay there after being sentenced to two-and-a-half years in jail for “spreading false information”—that is to say, passing friends copies of an online newspaper that Syria's government doesn't like.

Four other Syrians have also spent the past year in jail for internet offences, such as showing photographs of anti-government demonstrations that officially never took place. The severity may seem odd, since Syria's president, Bashar Assad, led the country's main internet club before he got his current job.

Syria is not the only Arab state with a hyperactive cyberpolice. Tunisians jokingly call the worldwide web the inter-nyet, and with good reason. As in Syria, all the country's service-providers are run by either the government or the president's relatives. Owners of internet cafés must keep careful records of their customers. Many websites, including such dangerous outlets as Yahoo! and Hotmail, are banned.

Zouhair Yahyoui knows just how dangerous. Before being released last November, he spent 18 months in prison for the sin of running the country's most popular dissident website, Tunezine. In April, a Tunisian court sentenced six young men to between 19 and 26 years in prison for downloading what prosecutors said was “terrorist” material.

Unlike Tunisia (or Saudi Arabia, which has blocked some 400,000 websites), Egypt does not censor the net. Its plan to get more people to use it by allowing cheap internet access is justly hailed as a model. But its special cyberpolice taskforce is vigilant, especially in trapping homosexual men by posing online as potential mates. Lured to some public meeting place, the lovelorn gays find themselves clapped in irons and charged with “debauchery”.

Even so, the internet is having a profound impact on closed Arab societies as a forum for minority and dissident views. Though long shut in by UN economic sanctions, and by the stifling censorship of its press, at least a fifth of Libya's 5m people now use the internet; either by incompetence or choice, the country's rulers have failed to block the dozens of sites that mock, question and insult them. Although the Saudi authorities' firewalls are massive, al-Qaeda's operatives in the kingdom still manage to use the internet as their main mode of communication and propaganda. And, though Syria's police are mean to political dissidents, they are nice to software pirates. For just a dollar, you can buy a programme off the streets of Damascus to cover your internet tracks—and safely get a look at all the forbidden stuff.

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Israel and Palestine

Move that wall

Jul 8th 2004 | EAST JERUSALEM
From The Economist print edition

The lawyers speak. The two peoples continue their quarrel

THE Israelis and the Palestinians are steeling themselves for another war over turf. The terrain this time is not just the Gaza strip, where the Israeli army and Palestinian fighters are engaged in a deadly war of attrition to determine whether the decision of Israel's prime minister, Ariel Sharon, to withdraw from it will look like a humiliating flight (as many Israelis fear) or as a clever tactic (as most Palestinians fear) to help Israelis consolidate their territorial grip over the West Bank. This turf war is also being fought by lawyers—in Israel's High Court and at the International Court of Justice (ICJ) at The Hague.

Last December the United Nations asked the ICJ to issue an advisory opinion on a barrier—a phalanx of walls, fences, trenches, razor wire and patrol roads—that Israel has been building down the length of the West Bank, with 185km (115 miles) out of a planned 630km already complete; so far, 12km of the barrier, especially where it curls round Palestinian towns, consists of a wall made of concrete slabs, eight-to-nine metres high; for most of its length, it is a barbed-wire fence varying in width from 60 to 100 metres, with a patrol road along the side closer to Israel.

Will it ever come down again?

Israelis say its purpose is purely for security, to prevent Palestinian suicide-bombers from entering Israel—and claim that it has already proved its worth. The government says that there have been almost no suicide bombings from those areas of the West Bank where the barrier is now up. But since its route in many places penetrates deep into the West Bank, to protect the biggest Jewish settlements there, the Palestinians see it largely as a land grab that would prevent the Palestinians from ever having a viable state, since it has the effect of carving their territory into shrinking and tenuously connected enclaves.

The ICJ was due to deliver its judgment on July 9th, after *The Economist* went to press. The Palestinians hoped it would declare the barrier illegal. The Israeli government said in advance that it would ignore the ICJ's decision. Israel is also trying to persuade the United States and European countries not to back a Palestinian-inspired resolution in the UN'S General Assembly that is sure to call on Israel to pull the wall down if the ICJ verdict goes against Israel.

Both Israel and the Palestinians have already taken heart from a ruling by Israel's High Court of Justice on June 30th that three-quarters of a 40km stretch of the barrier in the West Bank must be rerouted due to the “severe and acute way” it “injures” the 35,000-odd Palestinians living in its path. Mr Sharon said he would abide by this ruling, largely because the court upheld the Israeli government's basic claim that the barrier's main and legitimate purpose is for security. “It is a significant, suitable and authoritative judicial response to the false charges being brought against us in the ICJ in The Hague,” he said.

Still, the Israeli court's decision could set an awkward precedent for other segments of the barrier about to be built. Last month Israel began to build a barrier around Ariel, a large Jewish settlement 20km inside the West Bank, that will—says Israel's defence ministry—be joined to the main north-south barrier next year. The ministry says that the Israeli court's decision is unlikely to affect the route around Ariel and three other nearby settlements because they are “home to 50,000 Israelis and just one Palestinian family”.

Nonsense, retort the Palestinians. Some 11,000 of them in three West Bank villages have already had some more of their lands requisitioned to make room for the Ariel barrier. One village, Zawiya, may lose most of its nearby farmland. In recent weeks Palestinian and Israeli campaigners against the barrier have clashed with Israeli forces outside the village.

But the real test will be East Jerusalem, the Arab-populated part of the ancient city that has been occupied (and much of it annexed) by Israel since its victory in the 1967 war. If the route of the Israeli wall follows the latest maps issued by the defence ministry, it will bar or massively restrict some 200,000 Palestinians seeking to reach their lands, jobs, families, schools and hospitals, as well as holy sites in East Jerusalem. Many thousands of them are residents of Jerusalem forced to live outside the city limits because the Israeli-controlled municipality refused to let them build homes within them. They hope that the Israeli court's verdict on the route through part of the West Bank will apply to East Jerusalem as well.

This is why the Palestinians look so eagerly to the ICJ's ruling. They think that, combined with the Israeli court's decision, it should lend moral weight to their argument that, if the wall has to be built at all, it should go as close as possible to the “green line” that separated Jordan from Israel before the 1967 war. Where it cannot follow that line, for instance in East Jerusalem, it should not be built at all. Otherwise one of the two peoples who claim Jerusalem as their ancestral home and capital will be denied the right to live and move freely within it. But for many Israelis, security is paramount. A recent poll found that 78% support building the barrier, and only 16% are against. A lot of its supporters will feel that a wall with a big gap in it is not much of a barrier.

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Kenya

Scandals then and now

Jul 8th 2004 | NAIROBI
From The Economist print edition

Is Kenya's reformist government losing its way?

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AP

Falling out of love, again

THE protesters threw stones and set fire to tyres. The police responded with live bullets. Two people were killed and several injured. It was the worst week of political violence since Mwai Kibaki took over as president of Kenya from the reviled Daniel arap Moi 18 months ago.

There was euphoria when voters tossed out Mr Moi. His regime was blatantly predatory: its members used their power to rob Kenyans of their land, savings and sometimes, allegedly, their chastity. Mr Kibaki promised to end such abuses. At first, he seemed to deliver.

He stamped hard on police corruption and swept away rotten judges. In a survey for Transparency International, an anti-corruption watchdog, Kenyans reported that they were asked for bribes during only 40% of encounters with officials, down from 65% under Mr Moi. Mr Kibaki also made primary education free for all, which led to overcrowded classrooms but greater opportunities for the poor.

That early euphoria has now dulled, however. Mr Kibaki promised to introduce, within 100 days of assuming power, a new constitution that would trim the powers of the over-mighty presidency. He did not keep his word. His latest self-imposed deadline expired on June 30th.

Suffering from ill health, Mr Kibaki has allowed himself to be swayed by a cabal of controversial politicians from his Kikuyu tribe, Kenya's largest. This cabal, known as the Mount Kenya mafia, is said to be reluctant to share power with other tribes. It was at its urging, allegedly, that rallies this week protesting against the slow pace of reform were banned, a tactic common in the Moi years, as was the police's brutality against the demonstrators.

Foreign donors, who had welcomed Mr Kibaki's inauguration with open wallets, are feeling uneasy. Mr Kibaki reshuffled his cabinet last week, demoting critically-minded colleagues and promoting less desirable types. Kalonzo Musyoka, the popular and competent foreign minister, was moved downstairs. Moi-era hacks were brought back. An attempt to muzzle the anti-corruption tsar was only rescinded under pressure from donors.

Perhaps fortunately for Mr Kibaki, an inquiry into a big scandal of the Moi era is currently enthralling the nation. The scandal centres on a firm called Goldenberg International, which claimed a great deal of money from the central bank in export compensation for allegedly fictitious gold and diamonds. This and related scams are estimated to have cost Kenya $1.7 billion.

Kroll, a British firm hired to recover money stolen under the old regime, says it has already traced some of the $3 billion-plus stashed abroad by Mr Moi's cronies. And Kenyans are enjoying seeing the recently powerful squirm. In the witness stand for nearly a month, Kamlesh Pattni, a Goldenberg shareholder, has been telling some interesting tales. This week he handed judges a list of 1,200 senior officials—cabinet ministers, MPs, businessmen, civil servants and journalists—who he says benefited from his largesse. He claims to have plied one minister with Chivas Regal whisky before handing him a wad of cash to buy a

house. Officials say they have a tape showing him loosening up another minister with a gift of mangoes. “This is better than Big Brother,” said one Kenyan, gleefully watching proceedings in a crowded pub.

Mr Pattni's most sensational allegation is that the largest shareholder in Goldenberg was none other than Mr Moi. Mr Pattni says that, on his first visit to Mr Moi's luxurious residence, he was advised to bring a gift. “I thought he was suggesting that perhaps I carry a gold pen set or perhaps a gold tie pin,” Mr Pattni told the inquiry. He says he was told that $140,000 stuffed into a suitcase would be more appropriate. Mr Moi denies all wrongdoing.

All this has distracted only slightly from Mr Kibaki's woes. This week, the United States, Britain, the European Union and Japan threatened to suspend lending because of a new scandal involving a rather costly contract to produce Kenyan passports. Donors are also thought to be demanding the removal of the finance minister, a key ally of Mr Kibaki and leading Kikuyu politician. If Mr Kibaki cannot resuscitate his reforms, Kenya risks becoming a pariah once again.

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Italian politics

Berlusconi risks his bacon

Jul 8th 2004 | ROME
From The Economist print edition

The prime minister's accession to the finance ministry has neither eased tensions within his coalition nor stopped a rating downgrade

Get article background

A NEW biography of Silvio Berlusconi's wife reveals that her husband owns a collection of Napoleon figurines. Italy's prime minister may not have crowned himself emperor yet, but this week he took another step towards emulating his hero when he took control of economic policy. The country's head of government, richest man and owner of its three main commercial TV stations is now, even if only temporarily, finance minister as well.

This is not just bizarre, but perilous as well. That was underlined on July 7th when, alarmed by Mr Berlusconi's self-appointment and his high-risk plans, Standard & Poor's, a rating agency, cut Italy's long-term debt rating to AA-. This downgrade, which could sharply raise the cost of servicing Italy's huge debt, is the first to hit a member of the euro since the single currency's creation in 1999.

Until S&P's announcement, Mr Berlusconi was smugly hoping to have turned the tables on his adversaries in the government. His coalition has been cracking along a fault line that was always visible. In one camp are the prime minister's Forza Italia party and the Northern League, which both sprang from the north and broadly back liberalisation and constitutional reform to decentralise power. In the other are Gianfranco Fini's National Alliance, mainly composed of former neo-fascists, and the Union of Centre Democrats, largely consisting of former Christian Democrats, led by Marco Follini. These two parties, more reliant for votes on the poorer south and centre, are warier of liberalisation and fretful that decentralisation could widen the gap between south and north.

For some time, the hate-target of the second camp has been Giulio Tremonti, Forza Italia's acid-tongued finance minister, who shut them out of discussions, made policies they disliked and announced them without consultation. The biggest shock came in late March, when an ambitious plan for tax cuts was unveiled. Mr Fini and Mr Follini saw this as a blueprint for enriching northerners, using the proceeds of spending cuts that would fall heavily on their southern supporters.

After a miserable showing by Forza Italia in the European elections on June 13th, and in municipal and provincial ones two weeks later, Mr Fini felt emboldened to settle scores. Under growing pressure in his own party to pick off the finance minister, he made his move at a rancorous cabinet meeting on July 2nd, apparently saying to Mr Berlusconi “it's him or me.” The plan was for Mr Berlusconi to fire Mr Tremonti, which he did, and then hire Mario Monti, the highly respected EU competition commissioner. But Mr Monti declined. And by then Mr Berlusconi had made himself interim finance minister, although some advisers are still suggesting a new appointment will soon be made.

The risk was that an end to Mr Tremonti could also have spelt an end to Mr Berlusconi's promised tax cuts. The prime minister had already vowed that, if he failed to deliver them, he would not bother standing at the next general election. As his party's spokesman, Sandro Bondi, now puts it: “Who better than the prime minister to guarantee that this government's economic programme and fiscal reform are enacted?” Mr Fini and Mr Follini may find it harder to snipe at the prime minister than at his erstwhile finance minister—though this week's news that two of Mr Berlusconi's children are being investigated for alleged money laundering may make him more vulnerable.

Mr Berlusconi's extra job also offered temptations for his other role as media tycoon. Since the ownership of Italy's public broadcaster, the RAI, is vested in the treasury, he now has the power to dictate the financial policies of his main business rival and even to choose its chairman. “I like this job a lot,” Mr Berlusconi beamed after his first public engagement, a meeting in Brussels at which he persuaded fellow euro finance ministers not to give Italy an early warning for busting the stability-pact ceiling on budget deficits of 3% of GDP.

Even if Mr Berlusconi were a credible economic overlord, which he is not, he would still be a temporary, part-time one. And Italy's economic difficulties do not admit of temporary, part-time attention. The biggest criticism of Mr Tremonti has nothing to do with tax cuts, and everything to do with a failure to push through measures to tackle the structural weaknesses of the Italian economy. Handed a rare absolute parliamentary majority by voters, Italy's conservatives had an historic opportunity that has now been largely squandered. Three years into the Berlusconi government, there has been no pension reform, limited debt reduction, only modest privatisation and no growth-inducing jolts on either the demand or the supply side. These failings help to explain why Italy has been the most sluggish of the G8 rich countries to recover from recession.

The question now is whether Italy can afford the tax cuts its unexpected new finance minister wants. Can a country with a stagnant economy, public debt well in excess of GDP and under the (at least notional) constraints of the euro's stability pact, consciously forgo so much revenue? Standard & Poor's says the answer is “no”. But it remains to be seen whether that will deter Mr Berlusconi from pressing ahead with a policy on which he has staked his political survival.

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Greece and the Olympics

Torch-bearers

Jul 8th 2004 | ATHENS
From The Economist print edition

After winning Euro 2004, the Greeks look forward to the Olympics

Reuters

Soaring, worrying

IT WAS a fairy-tale ending that Greeks could scarcely have dreamt of. Their team arrived at Euro 2004 in Portugal as rank 80-1 outsiders. Winning the championship marked a success without parallel in Greece's recent sporting history. Over 200,000 delirious fans turned out to give their team a heroes' welcome, overflowing the stadium built for the first modern Olympics in 1896. With Athens preparing to host the Olympics again in only five weeks' time, the victory could not have been better timed. Costas Karamanlis, the prime minister, called it “the best possible invitation to the games.” The feel-good factor may make Greeks more confident of making a success of the Olympics. They might even improve on their 13-medal haul from Sydney in 2000.

Preparations for the 17-day Olympics have been fraught with anxiety. Missed deadlines for stadiums and transport projects, and worries about the Greeks' ability to handle security, have made the International Olympic Committee (IOC) wonder if small countries should ever host the Olympics. Jacques Rogge, the IOC president, has said that future games should be awarded only to cities that already have most infrastructure in place.

Greece's €4.6 billion ($5.6 billion) government budget for the Olympics is likely to overshoot by at least €1.5 billion. The security budget tripled after September 11th. Political infighting delayed decision-making, sending costs soaring. Inefficient tendering gave contractors a chance to squeeze more money out by foot-dragging. But the pace picked up when Mr Karamanlis's centre-right New Democracy party ousted the Socialists after last March's elections. Co-operation between the government and Athoc, the games' organising body, improved. Gianna Angelopoulos-Daskalaki, the Athoc boss, is a former New Democracy MP with an open line to Mr Karamanlis, who has taken overall ministerial responsibility for the Olympics.

With the 35 sports venues more-or-less complete, security arrangements are now the biggest headache. Sensibly, Mr Karamanlis adopted a plan from his Socialist predecessors under which Greece's NATO partners will provide AWACS aircraft to monitor Greek airspace, plus ships to patrol in the Adriatic and Aegean. A committee of foreign security advisers includes Americans, Britons and Israelis. An American company has a contract to co-ordinate security at more than 100 Olympic sites. But it is behind schedule in installing equipment and in training operators. With less electronic protection, the onus will fall more heavily on Greece's 70,000 police, soldiers and emergency workers.

Faced with traffic restrictions and a ban on summer holidays for civil servants and bank staff, to say nothing of the burden on taxpayers, many Athenians already wonder if it was all worthwhile. Ticket sales have been slow, though the average price is lower than at Sydney. American tourists are staying away for fear of terrorist attacks, say travel agents. Yet Athens will be a better place after the games. As Mrs Daskalaki points out, Greece has built 20 years' worth of new infrastructure in one go. The stadiums, mostly clustered in low-income neighbourhoods and around the old airport, will become leisure centres that, she hopes, might encourage the young to excel at sport. New highways, a suburban train and a tram system should reduce traffic jams and pollution. And pedestrian walkways around the city's classical monuments will add to their appeal. The main sports complex, with roofs and public spaces designed by Santiago Calatrava, a Spanish architect, should become a tourist attraction in its own right.

Corporate sponsors and the IOC are still holding their breath. Even if things go well, a glitch-free games seems unlikely. But if Mr Karamanlis is right and the Greeks' achievement in Portugal triggers a last-minute wave of Olympic visitors, a shinier, more self-confident Athens could become a trendy European city—even if the price will have been high.

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AIDS in Russia

In sickness and in chaos

Jul 8th 2004 | MOSCOW AND ST PETERSBURG
From The Economist print edition

Russia wins some serious money to fight AIDS. But it could go to waste

Get article background

Expensive lines of treatment

WITH perhaps a million Russians carrying HIV, but just $4.2m in the government's annual AIDS budget, it should be good news that the Global Fund has granted Russia some $120m over five years to fight the disease. Two-thirds is for buying drugs, which should allow up to 50,000 people to be treated by 2009. A mere 1,500 are in treatment now, though the World Health Organisation (WHO) reckons nearly 60,000 need it. Yet the biggest problem is not shortage of money. Russia has conflicts between departments and clinics, no agreed policies for testing and treatment, and no clear picture of how AIDS is evolving. It also seems not to care about cutting the cost of treatment. Unless these things are sorted out, the Global Fund's money could go down a black hole.

The grant assumes that a standard “first-line” cocktail of three drugs will cost $2,000 a year, and a more sophisticated “second-line” package $3,000. By 2008 it should be just $500-800. The government's budget should rise to $20m by 2006 and $54m by 2009. Yet last year the Russian health ministry was paying nearly $8,000 for a typical first-line package. That is not only more than the same drugs cost in America but, more strangely, about one-quarter more than typical retail prices at Moscow pharmacies or over the internet. And the federal budget is not set to change until 2006 at the earliest.

Drug firms are said to have promised to cut prices if patient numbers grow. But the only thing that can force them down is competition from cheaper generics. These are used in many poorer countries, and most are on the WHO's “prequalified” list, so that countries can approve them faster. But Russia has registered only one locally made generic so far. CIPLA, an Indian generic maker, says that approval in other countries takes 12-18 months. In Russia it has been trying to register one drug for nearly three years and several others for two years. That, says CIPLA, is because the health ministry insists on a declaration that the drugs do not infringe the original patents. Yet other countries dealing with AIDS have waived patent protection, a practice allowed by the WTO, which Russia hopes to join next year.

One problem with generics may be resistance from Russian doctors. “I don't know how well generics work,” says Yevgenia Sinchik, at the St Petersburg AIDS clinic. “We're not a third-world country, so we should try to meet world standards.” Aleksei Mazus, director of the Moscow AIDS centre, is more categorical: “Do these people understand the difference between normal medicines and fakes?”

Another dispute is over whom to treat. The Global Fund grant is aimed at “vulnerable” groups, among them drug addicts and sex workers. In the West HIV has spread mostly through sex; in Russia over 80% of people have caught it from dirty needles. But addicts often fail to stick to the strict drug regime, which can lead to drug-resistant strains. Dr Mazus argues that the grant is misdirected, and that only ex-users who can show they have kicked the habit should be treated. Yet he also claims that, in Moscow, everyone who needs treatment, including addicts, gets it. But that is still only 1,000 people. At least five times that number should be getting treatment if the WHO's nationwide estimate of 60,000 infected people is right. Are the others being ignored? Or avoiding doctors and tests, because they know they will be?

The statistics are clouded by bureaucratic rivalries. Officially 283,000 are registered with HIV, but that does not include new cases from Moscow for the past year thanks to a dispute over data. A decision to

move the cost of HIV testing from federal to regional budgets has, says Vinay Saldanha of the Canada AIDS Russia Project, led to “a very splotchy epidemiological portrait”. Poorer regions do fewer tests and neglect hard-to-reach groups like drug users. That produces wild variations: in some places the infection rate seems to be falling, in some HIV seems to spread mainly through heterosexual sex, and nobody can say how far AIDS has spread into the population as a whole.

Another controversy concerns “harm reduction”, notably the policy of giving addicts free clean needles to slow the spread of HIV. Dr Mazus says this can encourage non-drug-users to try drugs. He has similar doubts about “safer-sex” education: “What kind of approach is that to something that is such a serious relationship between people?” Again, he is not alone. A big AIDS conference in St Petersburg in May, took a stand against harm reduction, in a city that has one of Russia's biggest needle-exchange programmes.

With its population already declining fast, Russia cannot ignore AIDS. A World Bank study two years ago predicted that, by 2020, the effect of AIDS on the budget and the workforce could lop a full percentage point off annual GDP growth. Yet President Vladimir Putin has given AIDS only the briefest mention in public. An outgoing deputy health minister, Gennady Anishchenko, is taking the AIDS brief to his new job as head of the consumer-protection agency. That hardly makes this lethal epidemic seem a top priority.

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AIDS in Ukraine

Lobbying for life

Jul 8th 2004 | KIEV
From The Economist print edition

A country that is tackling AIDS with at least some seriousness

Get article background

IT IS a long hike up to the 19th-floor office of the All-Ukraine Network of People Living with HIV/AIDS. In a spectacular example of cutting its nose off to spite its face, the residents of the building have stopped the lift going above the eighth floor, in an effort to force the activists out. Yet despite such inconveniences, the organisation is abuzz with energy. And with good reason. Russians tend to sneer at Ukrainians as poor, backward cousins; but unlike Russia, where AIDS risks being overlooked (see article), Ukraine is taking the threat seriously.

Part of the reason, says Hannah Khodas, the network's programme manager, is that Ukraine is smaller: no similar group in Russia has offices in half the country's regions. And because Russia's bigger cities have the money to buy antiretroviral drugs for everyone who needs them, there has been less of a direct motive for civil activism. But another big factor is support from the top. President Leonid Kuchma's glamorous daughter, Olena Franchuk, runs an AIDS charity. Top stars have been persuaded to pose with HIV-positive friends for advertising campaigns. Before Russia could even get its act together to apply, Ukraine had won a grant from the Global Fund.

Less gloriously, Ukraine was also the first country to have its grant suspended, after the agencies in charge of spending it—among them the local office of the UN Development Programme—took too long to get going. Things have improved since a foreign organisation, the International HIV/AIDS Alliance, was put in charge. But there are still problems: on three occasions, private donors have had to fly in with suitcases and boxes full of drugs because the health ministry has not bought medicines in time. Only 137 people are on treatment, as against the 2,000 who need it. But that target is several times higher than originally planned, thanks partly to lobbying by activists. Their Russian counterparts can only dream of having that much influence over their government.

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The Milosevic trial

The show goes on

Jul 8th 2004
From The Economist print edition

Slobodan Milosevic is fit enough for trial, but maybe not to defend himself

Get article background

THE first head of state since the second world war to face charges of war crimes and genocide will not escape justice—as some had feared and others, including many Serbs, had hoped. The International Criminal Tribunal for the former Yugoslavia (ICTY) in The Hague ruled this week that Slobodan Milosevic was fit to stand trial, despite his deteriorating health. But the three-judge panel added that he might not be fit enough to continue to represent himself. It has ordered an examination by an independent cardiologist next week; it will then decide whether to impose a defence lawyer on Mr Milosevic, over his fierce objections.

The former Yugoslav president, who is 62, was due to open his defence on July 5th, after a four-month break to give him time to prepare his case. But proceedings were adjourned after doctors said that he was suffering from extremely high blood pressure and needed a rest. The lawyer assigned to ensure a fair hearing questioned whether Mr Milosevic was fit to stand trial at all. From its outset, the two-year-long trial has been plagued by repeated interruptions due to Mr Milosevic's ill health. To allow him to continue to defend himself could cause further costly delays, the court fears.

Set up in 1993, the ICTY was the first international war-crimes tribunal to be created since the Nuremberg and Tokyo tribunals after the second world war. But with a budget of $120m a year, it has been criticised for being too bureaucratic, too expensive and too slow, as well as too far removed from the victims in the countries from former Yugoslavia.

The court has now streamlined proceedings, cutting the number of charges brought against defendants—Mr Milosevic is facing 66—and conducting as many as six trials at a time. Under a “completion strategy” agreed with the UN Security Council, it has also undertaken to complete all investigations by the end of this year, all trials by the end of 2008, and all appeals by the end of 2010. But addressing the council last week, Theodor Meron, the court's president, and Carla del Ponte, its chief prosecutor, cast doubt on the court's ability to meet these deadlines unless certain “big challenges” were overcome. These included the court's “dire” financial situation, involving a total freeze on staff recruitment; its inability to transfer some less important cases to domestic courts in ex-Yugoslavia for want of sufficient guarantees that the trials would be conducted to international standards; and the lack of co-operation from Serbia and the Serb Republic in Bosnia in hunting down the 22 indictees still at large.

Mrs del Ponte has accused Belgrade of providing a “safe haven” for the fugitives. Radovan Karadzic, the former Bosnian Serb leader, and Ratko Mladic, the general charged with organising the 1995 Srebrenica massacre, have been on the run for almost ten years. “How long will it be tolerated that they make a parody of both justice and the repeated commitment of the Security Council to have them arrested and tried?” she demanded. She fears that protective networks in Serbia and elsewhere are trying to buy time until the 2008 deadline for the completion of trials, and has asked the council for reassurance that the court will be kept open for as long as it took to bring the fugitives to justice.

Depending on Mr Milosevic's state of health, the hearings in his case will resume on July 14th, but only for a week. The court will then adjourn until August 31st to give Mr Milosevic yet more time for his defence. Among the 1,631 witnesses he plans to call—five times as many as the prosecution—are such big shots as Bill Clinton, Tony Blair and Gerhard Schröder. Contrary to normal practice, the court has decided not to restrict the list to those likely to provide relevant evidence. Instead, it will leave it up to Mr Milosevic to decide which witnesses to call—provided he completes his defence within 150 court days. Some interesting scenes could yet be played out in The Hague courtroom.

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Danish immigration laws

Love bridge to Sweden

Jul 8th 2004 | COPENHAGEN AND MALMO
From The Economist print edition

One consequence of Europe's toughest immigration laws

LAST week marked the second anniversary of what the Danish government boasts are the European Union's strictest immigration laws. But Christina Reves, a 23-year-old estate agent, was not celebrating. For the laws have driven Ms Reves and many other Danes with spouses from non-EU countries into involuntary exile in Sweden.

Danes may tie the knot with anyone (same-sex marriages included), but getting a foreign spouse into the country is harder. To get a residence permit, both partners must be 24 or over. They must pass a solvency test, showing the Dane has not drawn welfare benefits for the previous 12 months, can lodge a bond of DKr53,000 ($8,700), and can earn enough to support his or her spouse. The pair must have a permanent home (no staying with family) and—the crunch for many brown-skinned Danes—be judged to have ties to Denmark exceeding those to any other country.

In 2001, before the new rules came into force, some 13,000 family “reunification residence permits” were granted. In 2003 fewer than 5,000 were. Many who failed have found refuge in Sweden. EU laws on the free movement of workers let Danes, with their foreign spouses, take up residence in Sweden. Many keep jobs in Copenhagen. The new bridge across the Oresund makes cross-border commuting easy—if expensive. Sweden's more relaxed regime offers another loophole: Danes can qualify for Swedish passports after only two years' residence. Armed with a Swedish passport, former Danes can use EU laws to return home—with their spouses.

Yet even if it can be surmounted, the web of complications and barriers has made the exiles angry. A group of Danes recently gathered on Malmo's main square to protest, saying they felt hurt and betrayed. They also expressed deep gratitude to their Swedish neighbours. “I'm very grateful to Sweden. I know they had to take me but they were extremely welcoming,” says Ms Reves, who now lives in a Malmo apartment with her Egyptian husband. As many as 1,000 couples have now crossed the love bridge. The Swedish migration board reckons that Danes are arriving at a rate of 60 couples a month. The exodus could one day even exceed the country's previous migration record, set in 1943, when more than 7,000 Danish Jews were spirited across the Oresund to escape the Nazis. Then, as now, Danes found welcome refuge in Sweden.

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By invitation

Jack Straw

Jul 8th 2004
From The Economist print edition

Charlemagne steps aside to let Britain's foreign secretary reply to our leader on the European Union constitution

Get article background

AS WITH the winner of Euro 2004, I got one prediction about the new European Union constitution wrong. Writing in *The Economist* 21 months ago (see article), I suggested that, like the UN Charter or the US constitution, a pocket-sized document would be a signal of its coherence. Well, at 626 grams and 325 pages, you need a poacher's pocket, so it does not quite pass that test. But hang on. Compare what the EU has now with what it will get in the new constitution, and the document passes with flying colours.

First, it is far more coherent than its predecessors. At present, the EU is governed by two sets of overlapping treaties, providing for “three pillars”, several different ways of producing laws and a voting system that lacks a rational basis (Germany, with almost twice Spain's population, has just 7% more votes). There is no clear statement of what the EU is or what it does. Some absolutely fundamental principles, from the primacy of EU law to its exclusive competence over marine conservation, are not mentioned in the treaties. Now, set out in part I of the constitution, is what the EU has needed for years: clarity and coherence about where its powers come from, and how decisions are made. And, at just 59 short articles, this part, which sets the framework for the Union, could easily fit into anyone's pocket.

The constitution dispatches into oblivion any notion that the EU is a federal superstate. It is the member states that confer competences (powers) on the Union “to attain objectives they [ie, the member states] have in common” (article 1). “Conferral”, meaning that the EU's powers derive from member states, is a fundamental principle, requiring the EU to act “within the limits of the competences conferred upon it by the member states”. Competences not so conferred remain national. And there is even a streamlined procedure, for the first time, for any member state to withdraw from the EU—proof, if more were needed, that this is an organisation of freely co-operating nations.

The EU's reputation has suffered in the past because the use and transfer of powers has appeared to be a one-way street. Now, there are innovations in the constitution that can make it two-way. Shared competences (or part of them) can be transferred back to member states (article 11). And national parliaments are charged with the duty of ensuring compliance with the principle of subsidiarity.

In its leader of June 26th, *The Economist* dismissed the procedure for subsidiarity; but it was wrong to do so. At present, there is no obligation on member states or the European Commission even to inform national parliaments about draft EU laws, still less to let them have any power. But under the new provisions all national parliaments must be notified independently of all draft laws, and given six weeks to respond. If a third of them object, the commission must “review” the draft. Yes, in theory, the commission could then re-submit the original proposals unamended, but in practice they would be unlikely to do so, not least because, if a third of national parliaments are against a proposal, so will be their governments, and the commission would be close to losing the qualified majority needed to pass laws.

The Economist also complains that the new treaty “does nothing to provide citizens with any sense of control over the process of European government.” But the new subsidiarity provision is there to be used. It is up to national parliaments, the most effective voices of Europe's citizens, to make it work.

The constitution also shifts power back to member states, and so citizens, in another way: by reform of the presidency system. This sounds a bit arcane. But imagine any complex organisation where the leadership had to switch every six months, and it was only your turn once every twelve-and-a-half years.

What would happen is that effective power would shift, automatically, to those with some permanence. And no imagination is needed: this is the EU today. Rotating the presidency made sense when the EU had six members. With 25, and soon to be more, it is now a recipe for member states to lose their grip. A key institutional reform creates a full-time post of president of the European Council (ie, heads of government) to put into effect its decisions on the EU's strategic direction. This was a British proposal. Also, the size of the commission is to be reduced.

A better draft

When the Convention on the Future of Europe published its draft constitution a year ago, *The Economist* took issue with it. So, in some respects, did we. But it is now much improved. Of 80 separate sets of amendments agreed in the inter-governmental conference, 39 were advocated by Britain. We achieved every one of the goals set in last September's white paper. Even *The Economist* concedes that decision-making will be easier and a “clear improvement on the previous arrangements”. So too is the voting system, where a simple formula of 55% of member states, comprising 65% of the EU's population, will in almost all cases make up a qualified majority.

Where *The Economist*'s analysis falls down is in its inference that it is the constitution alone that can deliver real progress in Europe. No constitution can do that by itself. This one does, however, provide a better platform for the EU to concentrate on where EU-wide engagement adds value—and to work better.

Here lies a paradox about the EU, and also the root of our collective ambiguity towards it. Were it a superstate, writing its constitution would be easy, and the result short. You would declare that power resided in its parliament, government and supreme court, and leave those institutions to make and enforce the law. It is precisely because the EU is not a superstate that it needs a more complicated rule-book spelling out, policy by policy, the areas of its competence. This is what gives this document its length, so confounding one (but only one) of my predictions. But overall, it is a good constitution, which sets the right framework for a reformed and effective EU, and deserves support.

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Correction: Boris Gryzlov

Jul 8th 2004
From The Economist print edition

In a story on the north Caucasus on June 26th, we wrongly identified Boris Gryzlov as Russia's interior minister. In fact, he is now chairman of the Duma, the lower house of parliament; the current interior minister is Rashid Nurgaliev. Sorry

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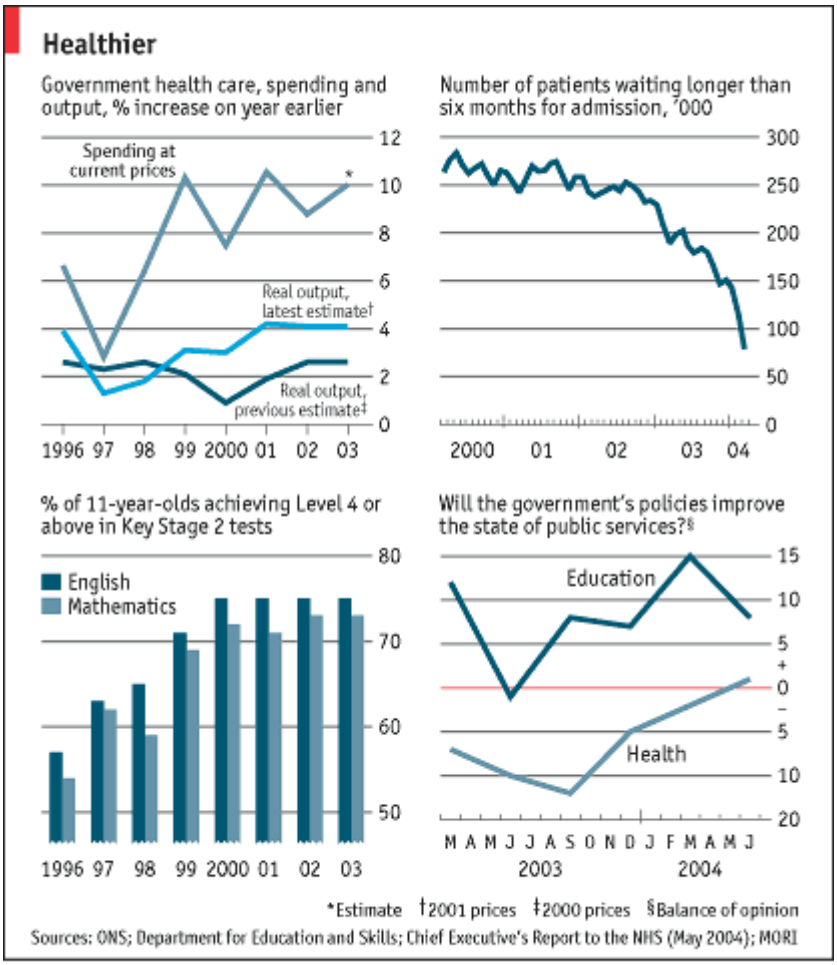
Public services

What good has the money done?

Jul 8th 2004
From The Economist print edition

Health and education are improving but not by enough to quell worries about whether taxpayers are getting value for money



Get article background

ON JULY 12th, Gordon Brown will unveil a new spending programme for the three years to 2007-08, which will thus span the election expected in the summer of 2005. In 2000, a year before the last election, he set out the government's spending plans in a similar way. But this will be a very different occasion.

Four years ago, the public finances were in the black and Mr Brown could draw upon the surplus to turn the spending geyser on full blast. This year, the government is running a big deficit and he is poised to turn the geyser off. Outside health and education, public spending will flow very slowly after spring 2006.

This alone makes for a rather different backcloth to the next election. As important, the government can no longer expect to be given the benefit of the doubt, as it was in the 2001 election, for what the spending bonanza might achieve. After several years of rapid growth, it has to point to concrete evidence that the extra money is delivering results, especially in health and education, the two public services that

voters care most about.

Until recently, the government's biggest headache was the National Health Service. As more money poured in, growth in hospital activity slowed down rather than increasing as expected. Productivity in the NHS appeared to be collapsing.

However, there is now a growing sense of confidence among ministers that the extra spending is starting to produce results. New official figures show that the extra cash has produced a greater volume of output from the NHS than was previously thought. Whereas the former estimates indicated an annual increase of 2% in the five years to 2003, the revised figures show that NHS output rose by nearly 4% a year.

And the government can point to other indicators of progress. The NHS has managed to cut the maximum waiting time for an operation from 18 to nine months. By next year, it should get that down to six. That period does not include the time spent waiting to see a hospital consultant after an initial referral, which can be as long as 17 weeks. But the government is now so confident about progress that it has pledged a maximum all-in wait of 18 weeks by 2008.

But whereas the NHS now seems to be on the mend after a long period of disappointing performance, the opposite seems to be the case in education. At the last election, Labour could point to rapid improvements in primary schools. In particular, there was a big rise in the proportion of 11-year-olds reaching expected standards in English and mathematics. But that improvement has levelled off despite big increases in school budgets.

In secondary schools, the record is mixed. On the one hand, there are record pass-rates for pupils taking GCSEs at 16 and A-levels at 18. On the other hand, the proportion of 19-year-olds with at least a “level 2 qualification”—such as one A-level or five or more GCSEs at grades A* to C—has only edged up from 74% in 1998 to 76% in 2003. Anyway, the row about dumbed-down exams means better results are viewed with scepticism.

A year ago, more people thought that the government would fail rather than succeed in improving health; now a narrow majority think it will succeed. However, people have recently become less optimistic about the government's chances of improving education.

Yet neither rating adds up to a resounding vote of confidence. With so much money being poured into the public services, there was bound to be some improvement. Labour remains vulnerable on the charge that it is failing to get value for money. For example, the gains in NHS output, though more respectable than previously estimated, still fall a long way short of the rise in its cash budget, which has been growing by nearly 10% a year.

The government could probably have achieved more with less if it had been more single-minded in its reforms. It is striking that the recent improvements in health follow the reintroduction of an internal market in the NHS, with hospitals starting to be paid by results. And the opening-up of the NHS market to new foreign health-care groups is achieving a lot more than the wish-lists of Labour's first term. If education is now lagging, that may be because the government has done too little to introduce market pressures.

So although people are noticing a bit of a difference, delayed and half-hearted reform means that the government is vulnerable to the accusation that much of the money has been wasted. Ministers will spend most of the next year trying to refute that charge.

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EU rebate

Too rich for a rebate

Jul 8th 2004
From The Economist print edition

The European Commission thinks Britain should pay more

ACCORDING to newspaper reports, the European Commission is preparing for an assault on the unique rebate, currently worth €4 billion ($5 billion), Britain receives to cut its net budget contribution to the European Union. From Tony Blair's point of view, as he struggles to win round voters ahead of a referendum on the European constitutional treaty, the timing could not be worse.

In one sense, however, the Commission's attention is quite flattering. When Margaret Thatcher famously got her money back 20 years ago at a summit in Fontainebleau, Britain was the third poorest country in what was then the EEC. She got it partly because it seemed unfair that a country so poor was the biggest net contributor. Now, on the basis of income per head, Britain is the richest big country in the EU (see chart).

What's more, Britain's rebate, which is set at two-thirds of its net contribution, is actually going up. This is because, thanks to this year's enlargement, EU spending that would previously have gone to poorer parts of Britain will now go to new members, such as Poland and Slovakia. The consequence is that, as a percentage of national income, Britain will soon pay in less than any other rich member country—0.25% according to the Commission, compared with 0.56% for the Netherlands, 0.54% for Germany and 0.37% for France.

Simply getting rid of Britain's rebate would be too draconian even for the Commission. If that happened, Britain's net contribution would soar to 0.62%. The Commission therefore proposes a new “mechanism” which would end the right to a rebate for any country that contributes less than a net 0.35% of GDP.

Having recently fought hard to retain its right to veto any change in its rebate, the British government is not likely to acquiesce meekly, particularly as the new arrangement would mean France once again doing much better than Britain because it continues to benefit from the common agricultural policy. Instead, expect Britain to demand further reform of the hated CAP in exchange for accepting the new mechanism.

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Religion

Blunkett's commandment

Jul 8th 2004
From The Economist print edition

The short path from faith to hatred

Reuters

Qaradawi: both respected and reviled

RELIGIOUS conflict, not much discussed in secular Britain for the past century or so, is back on the agenda. David Blunkett, the home secretary, wants to discourage it, while a controversial Muslim cleric's arrival threatens to arouse it.

Mr Blunkett wants to make it illegal to incite religious hatred. Muslim leaders are cheering him on. They say far-right groups denounce Islam with a vitriol that nobody would dare use against a race. Since stirring up religious hatred is against the law in Northern Ireland, why not extend this to the rest of Britain?

Reasonable as all this may sound, Mr Blunkett's proposal will meet stiff opposition. Secular libertarians point out that stirring up hatred can be hard to distinguish from stridently asserting the truth of one faith over another. Almost all the major religions have strong things to say about the fate of those led astray by other beliefs; could the mere repetition of these warnings to infidels become a crime?

But Mr Blunkett's reasons for promoting this legislation are not all to do with tolerance. In return for this concession, which is part of a broader horse-trading process, Muslim leaders are being urged to co-operate with the police and isolate extremists.

But is a “grand bargain” between the government and British Muslims, many of whom have abandoned the Labour Party, really on the cards? There are plenty of stumbling-blocks, not all to do with Iraq.

The arrival in Britain this week of Sheikh Yusuf al-Qaradawi, a spiritual leader of the Muslim Brotherhood and one of the world's top Islamic scholars, drew furious denunciations from some members of Parliament and the tabloid press. Sheikh Qaradawi is neither the most moderate, nor the most extreme, of Muslim clerics; he has vigorously condemned al-Qaeda's attacks in America and Indonesia (and won western plaudits for doing so) but condoned suicide bombings in the Middle East. His pronouncements on every subject from personal ablution to the status of Jerusalem are followed keenly by Muslims all over the world.

If the government decides to bar the Qatar-based cleric, it will enrage the most politically-active segment of British Islam: the leaders of the Muslim Association of Britain. They are ideologically aligned with the Muslim Brotherhood and recently launched—along with their powerful allies in France—a pan-European campaign to assert the right of women to wear the veil. Sheikh Qaradawi is one of their spiritual leaders. If his right to visit Britain is questioned, no legislative concessions will stave off the prospect of something uncomfortably like religious conflict.

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Divorce

Own goal

Jul 8th 2004
From The Economist print edition

Bad news for people with big salaries and grumpy spouses

PA

Karen got her cream

A NASTY blow to a British footballer has made English divorce courts more fearsome for rich spouses (and better for their poorer partners). On July 7th, the appeal court in London said that Ray Parlour, known to Arsenal supporters as the Romford Pele, would have to pay a third of his estimated £1.2m ($2.2m) annual income to his ex-wife.

In recent years, English judges have typically divided marital assets equally. That contrasts sharply with the practice in most of Europe, where the contribution made determines who gets what.

But judges divided income on needs, not fairness. Now, at least for households with high earnings and low savings, that may change. The judges accepted Karen Parlour's argument that her wifely discipline had helped her ex-husband's success on the field. She had weaned him off the boozy laddish outings that threatened his career, she said.

Recognising that the 31-year-old Mr Parlour's career will soon wind down, the court fixed payments for another four years only. Even that may be a stretch—his contract with Arsenal runs out next year. The big slice of those high earnings that his ex-wife now gains reflects not her current needs, but provision for her long-term future.

That's a step towards the way divorce works in New York, where careers are seen as businesses in which the other spouse is a shareholder. As a result, those with brief, lucrative careers may conclude that marriage is an unaffordable luxury; others may take early retirement if things get wobbly at home.

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Intelligence and Iraq

Waiting for Butler

Jul 8th 2004
From The Economist print edition

The Butler report is likely to be more embarrassing than damaging for Blair

Get article background

NEXT week will be another tricky one for Tony Blair. He is braced not only for a couple of unwelcome by-elections in safe Labour seats, but also for the publication of the Butler committee's report into the intelligence received before the Iraq war and the use made of it.

Lord Butler's investigation has so far generated none of the excitement that surrounded the Hutton Inquiry. That is partly because, while Lord Hutton opened a window into the heart of government, Lord Butler has taken evidence privately and discreetly. And, as a former cabinet secretary, he is seen as an establishment type who will be gentle with ministers and senior intelligence officers. The two main opposition parties' refusal to take up their places on the committee has further encouraged suspicion of a whitewash (although one independent-minded Tory MP, Michael Mates, has stayed the course).

Witnesses who have appeared before the committee report that, as well as examining the intelligence relating to Iraq, the committee has also looked at the problems of dealing with other rogue states bent on acquiring weapons of mass destruction (WMD). Any attempt to put the decisions leading up to the war in a wider context should be helpful to the prime minister. But witnesses have also expressed surprise at the intensity of the questioning and Lord Butler's willingness to follow the trail wherever it has led.

The report is expected to criticise both intelligence failures and the gung-ho way in which the government set about building a case on what turned out to be shaky foundations. Lord Butler, a stickler for process and properly-minuted meetings, is known to take a dim view of the informal, free-wheeling way in which Mr Blair operates. In the past, he has also warned of the dangers of blurring the roles of political advisers and civil servants.

It would thus be surprising if Lord Butler did not censure the excessive mateyness between Alastair Campbell, the now-departed Downing Street communications chief, and John Scarlett, the head of the Joint Intelligence Committee at the time. Mr Campbell has returned to journalism, but Mr Scarlett is about to become head of MI6. If Lord Butler came down hard on him, he would have to go, and that would embarrass Mr Blair. Lord Goldsmith, the attorney-general, is also vulnerable. It is said that he overcame his doubts about the legality of the war only at the last moment and after some arm-twisting.

Lord Butler had promised that, if he criticised anyone directly, he would warn them in advance. And, according to Whitehall gossip, none of those who has cause to fear the worst has been sent a warning letter. But that may be because the committee has not yet decided whether to pick on individuals.

There is talk that, if the report's publication goes badly for the government, Mr Blair might indicate regret that mistakes were made. Labour MPs are hoping for a commitment never again to go to war in such circumstances. On July 6th, while appearing before the parliamentary Liaison Committee, he conceded for the first time that WMD might never be found. But, given that he still believes that the war was justified, he is unlikely to apologise.

Unless Iraq turns into a catastrophe, it has already done its worst to Mr Blair's political reputation. Lord Butler should have interesting things to say about the way intelligence is processed and used, but his political impact may be limited. Most people made up their minds about Iraq long ago and won't change them now.

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Education

Who chooses what?

Jul 8th 2004
From The Economist print edition

More freedom for schools—but not for the things that really matter

Get article background

INDEPENDENCE sounds great—up to a point. The centrepiece of the government's new five-year plan for education, announced on July 8th, is to increase the number of independent state schools, and give them more freedom.

It sounds good. Almost every secondary school in the country will be encouraged to apply for “foundation status”—something currently enjoyed by only a few hundred. That will give more independence from local authorities in administration, staffing and finance—and also, now, in expansion. So popular schools will be able to take on more pupils. Local education bureaucracies usually try to stop this, in order to keep numbers up at less-favoured schools.

The worst of these will be closed and replaced by Academies—new, well-financed and independently managed schools. The government is trebling their number, to a planned 200 by 2010.

But the reality is more modest. For a start, most schools already run their own budgets. The days when bloated local education authorities micro-managed schools are a memory, not reality. The most burdensome bureaucracy for head teachers now comes from central government, not local officialdom. Some smaller schools actively dislike the idea of more independence, reckoning that they will waste time on administration that they would rather use for teaching.

On the two big issues—selection of nice pupils and expulsion of nasty ones, schools' freedom will still be very restricted. Schools may choose a few pupils on the basis of “aptitude”—“an entirely different thing from ability” says a senior government source firmly. But for the most part, they will still take a mix of pupils from their neighbourhood, according to rules set by the local education authority.

In fact, autonomy in admissions will shrink further. A new collection of measures on school discipline includes the idea that schools should group together and agree that each takes its “fair share” of disruptive pupils. That makes sense in educational terms: peer pressure is the strongest influence on behaviour, so a rowdy child in a calm school will behave better, while a bunch of badly behaved pupils will egg each other on.

But parents may see it differently. Fair shares are all very well, until a hell-child ends up in your own offspring's class. The government says schools will be able to get together to run joint “sin bins” and other arrangements for the worst pupils.

Further ideas in the same package include a move back to uniforms at all schools, and tougher measures against truancy. This is the headline-catching stuff that will help the government compete with the Tories' pledges of education vouchers and fee-free universities.

But the fundamental problem remains: wise parents want their child educated alongside brighter and nicer pupils, not dimmer and more disruptive ones. Deplorably selfish perhaps—but trying to work against it has created a ruthless struggle for places at good schools. Tony Blair wants to tempt the urban middle classes back into state education. But doing that without sacrificing Labour's non-selective ideal will be very difficult.

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Corporal punishment

Slapped down

Jul 8th 2004
From The Economist print edition

British worries over a ban on parental violence are misplaced

LAWS are like children's shoes: they are either out of date, in which case they pinch, or they are new and discomfiting. Tantrums resulted this week, when the House of Lords pondered a dusty 1860 law that allows parents to beat their children as long as they do not go beyond “reasonable chastisement”. A clear ban would have been unpopular, although the nation would probably have grown used to it. Polishing the old law, which is what the Lords decided to do, is a stopgap measure that annoys children's advocates and leaves Britain out of step with other countries.

That reform was on offer at all is mostly thanks to foreigners. In 1998, a 14-year-old boy told the European Court of Human Rights that the British courts had failed to protect him against his stepfather, who had beaten him with a cane. He won, and the government pledged to amend the law. Not surprisingly, though, nothing was done. Although opinions are slowly softening, polls continue to show solid majorities in favour of the right to smack, and the government does not want to seem intrusive. The Lords' decision is a compromise: parents will be able to physically discipline their children, but not bruise them.

Why not ban smacking altogether? Twelve other European countries have done so, either on principle or after harrying from the United Nations. Behaviour has changed as a result. In Germany, where the law was modified in 2000, surveys of 12-to-18-year-olds suggest a steep decline in severe treatment. In 1992, three out of ten children reported being beaten to the point of bruising; ten years later, the proportion was three in a hundred. Lest it be thought that Teutonic discipline had vanished overnight, children reported a rise in painful measures like television bans and hits to their pocket money.

Encouragingly, the mere threat of punishment has changed parental behaviour. Prosecutions for real violence and neglect have increased in some countries, but the stern hand of the state has not descended on millions of well-meaning European bottoms. Jesper Hjortenberg, a Danish public prosecutor, says that beatings rarely reach the courts, mostly because they are not reported (“children are usually very loyal to their parents”, he says) or simply not worth prosecuting.

Meanwhile, a legal mess is developing in countries that have tried to reconcile an increasingly intolerant attitude to violence with the principle of parents' rights. These nations have struggled to draw the line as to what is acceptable. Scotland considered a ban on hitting toddlers, and ended up barring assaults made with implements. Earlier this year, Canada decided that 3-to-12-year-olds could be hit, provided it wasn't on the head. But Canadian smacking must be corrective, and not the result of frustration or hot temper—a circumstance few parents will recognise.

Such shenanigans not only prove the reformers' argument that smacking is a matter of national habits, not universal child-rearing difficulties. They also make it harder for police, prosecutors and judges to exercise discretion. Oddest of all, they make lawmakers responsible for fine-tuning levels of acceptable violence in the home. A peculiar result, for those who fret about a nanny state.

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Road pricing

Hot ideas for slow traffic

Jul 8th 2004
From The Economist print edition

Britain's congested motorways will get bigger, but more expensive

ROAD space is underpriced, and therefore overused. But making drivers pay has long been a political hot potato. Encouraged by the success of central London's congestion charge, the government is now moving towards road pricing for Britain's overcrowded motorways.

The main idea is a new toll road. The government announced on July 6th provisional plans for a 50 mile (80 km) dual-lane motorway between Birmingham and Manchester. That links up to Britain's existing toll-road, which has cut traffic on the next-door motorway, the M6, by 10%.

Views differ. Most locals like the new road and support the extension, although the freight industry complains that the £10 toll for lorries is too high, compared with £2 for a car. More generally, the road lobby complains that drivers will "pay twice"—once through tolls, and again through taxes on fuel and vehicles. Environmentalists are cross too; they say the money should go into railways.

But the railways, despite being drenched in public money under this government, have failed to prove themselves a realistic alternative. The government hoped four years ago that rail passengers would increase by 50% in a decade. But that now looks like being a rise of only a quarter. An ambitious plan for a private freight-only railway from the north-west to the Channel Tunnel has got nowhere.

Simply widening existing motorways, as the road lobby has been demanding, looks pointless: new capacity breeds new demand. A new road does use more land, but it's cheaper and less disruptive to build. Toll revenues are a logical way of paying for both its construction, and road transport's indirect costs like pollution.

The difficulty is the details. Private operators like building and operating toll roads where they keep the profits. Governments prefer schemes that they can milk for public-transport subsidies. America, which needs to renew its interstate highways, is grappling with these questions now.

The government's other plan, special lanes for high-occupancy vehicles (HOV), also originates in America. These could come as part of a road-widening scheme, or from using the hard shoulder at the side of motorways.

They sound a reasonable idea. A mere 1.1 people travel in the average vehicle on a motorway in peak times. Squeezing them into fewer cars would cut congestion.

But, unless they carry an hourly 700-900 vehicles (which they usually don't), HOV lanes don't compete with ordinary lanes, says Pilo Willumsen, of Steer Davies Gleave, a consultancy. America is moving to "HOT lanes", useable also by single drivers willing to pay tolls that vary according to traffic. That puts economics in the driving seat, where it belongs.

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PFI

What went wrong with Jarvis

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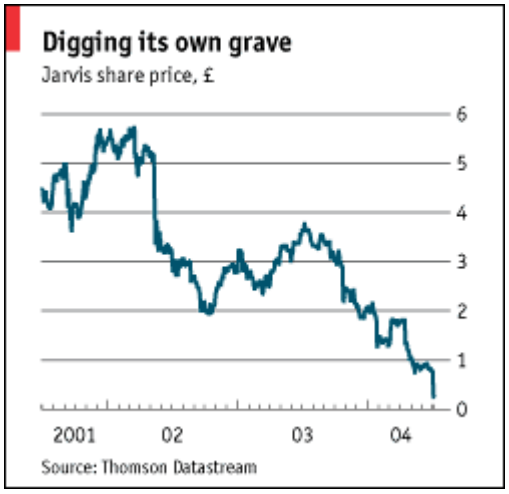
One company's woes don't damn the private finance initiative

JARVIS, one of the biggest contractors in the government's private finance initiative (PFI), has seen more publicity than the average building and rail-maintenance company is used to. It was blamed for the Potters Bar rail crash of May 2002; as a result, Steve Norris, company chairman since November, is reckoned to have sunk his chances of becoming Tory mayor of London by taking the job; and it is one of the main companies involved in the controversial public-private partnership now running London's Tube.



This week it had more unwelcome headlines. After three profit warnings (so far) this year, it admitted on July 2nd that its debt had soared £100m, to £230m, since April and that it faced £156m-worth of write-offs, on top of £40m of exceptional costs when it quit overground rail maintenance on March 31st. That has left the company, one push from the abyss, in the hands of its bankers.

Why? The trouble goes back to the days of Paris Moayedi, Jarvis's long-time chief executive and briefly chairman before he stepped down last year. At that time, Jarvis, with about £1.2 billion annual turnover, was bidding for contracts, worth, over time, some £12 billion. Bidding is a costly business, especially when the counterparties, as in the PFI, belong to the public sector. Jarvis did worse than spend heavily on bidding: too often, it won. On one calculation, it is now involved in PFI contracts totalling over £3.5 billion.

To win those contracts, Jarvis had to bid low, expand fast and hire sub-contractors extensively. There lies a classic recipe for trouble: overstretched management, shoddy work or delay, payment disputes with the client, and no huge reward ahead to keep bankers happy as time and costs mount. Worse still if the client pays on completion, as the public sector likes to; and even worse if the finance is heavily geared, as it usually is with PFI.

But an executive of another company experienced in the field says it is not the PFI's fault. Jarvis, he argues, bid for more than it could cope with. It has had trouble with clients over schools, from Kirklees in the north, westward to Wirral, down to Brighton in the south. In Norfolk it lately parted company with a building firm that it planned to use for a £260m-plus schools deal.

This arm of Jarvis has lost two chiefs in five months, and accounted for £115m of last week's bad news. On top of that, Jarvis will get only £30m of £56m that it says it expected from Network Rail, and more is in dispute. Even its seemingly trouble-free roads division has written off £15m.

Jarvis may survive. It could sell its Tube interests, but if it does, Transport for London could claim a share of profits from a price above £84m.

So what about the councils with whom Jarvis had contracted to build schools and the like? Their money wouldn't be down the pan: they owe only for value that they have had. But they will have to find other companies to finish jobs for them. That in itself will eat officials' time and may well cost more.

Jarvis's collapse may hit the PFI, too. Some of the banks that financed its schemes will lose money, and all may be shyer of PFI than they were.

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Bagehot

Not enough boots on the ground

Jul 8th 2004
From The Economist print edition

Britain's armed forces are getting an overdue shake-up, but the government doesn't want to talk about it

EVERYONE agrees that the next election will be fought over public services. The brawling about which party has the best ideas for education and health is already under way. But there is one public service on which taxpayers will spend the best part of £35 billion ($64 billion) next year, and which, if the government has anything to do with it, is destined to remain a surprisingly politics-free zone: defence.

After the end of the cold war and New Labour's renunciation of unilateral nuclear disarmament, defence, perhaps predictably, plummeted down the list of issues that matter to voters. In 1998, the Labour government produced its Strategic Defence Review, which marked the shift from preparing for a major war in Europe to structuring forces able to fight farther afield. Some questioned whether it would ever be implemented, but few quarrelled with its thinking.

Since then, Tony Blair has repeatedly called on the armed services to do his bidding. Soldiers have been dispatched to Kosovo, Sierra Leone, Afghanistan and Iraq. Mr Blair's readiness to use force for moral or humanitarian purposes is one of the defining characteristics of his premiership. He has also become a fervent admirer of Britain's small but highly professional armed forces.

Which makes it all the more unsatisfactory that there has been so little debate inside or outside government about what's happening to those armed forces. They are to be subject to big changes. The problem is not that the changes are wrong in themselves—they may not go far enough—but that they are being determined behind the closed doors of the Ministry of Defence with as little scrutiny as the government can contrive.

Last December's unforthcoming Defence White Paper talked about moving away from “simplistic platform-centric planning, to a fully ‘networked-enabled capability' able to exploit effects-based planning and operations”. But in 20 pages of jargon it could only hint at what that might mean. Last week the House of Commons Defence Committee lamented: “We are disappointed that an important policy document has been presented with little or no information on the relevant procurement decisions, funding questions or likely changes in force structures.”

Another sign of the times was the decision a couple of months ago of the defence secretary, Geoff Hoon, to replace the officers who traditionally head each service's PR department with civilian appointees who would be directly responsible to him. This little-noticed “reform” was generally seen within the ministry as a way of curbing the services' ability to make their views known to the outside world. After the mauling he received over the death of David Kelly and as the minister with operational responsibility for a war that has divided the country, Mr Hoon's reticence is understandable, but wrong.

Mr Hoon has been encouraged in his strategy of obfuscation by the bind the Tories have got themselves into over defence spending. Their spokesman, Nicholas Soames, a grandson of Winston Churchill and a former minister for the armed forces, is both knowledgeable and passionate. However, since Oliver Letwin, the shadow chancellor, announced spending plans that would mean no increase in the defence budget during the first four years of a Conservative government, Mr Soames has struggled to make an impact.

It's a fashion thing

What is worrying many defence experts is that the ministry, presented with the chance to rebalance

British forces for the roles they are likely to have to play over the next ten to 20 years, may be getting it wrong thanks to a potentially dangerous combination of timidity and trendiness.

The timidity takes the form of not taking a sharp-enough axe to procurement programmes conceived during the cold war, such as the Typhoon interceptor (commonly known as the Eurofighter), and activities such as hunting the North Atlantic for non-existent Russian submarines with expensive Type 23 frigates and upgraded Nimrod aircraft. The Typhoon, designed to win air superiority in Europe, is an over-sophisticated anachronism. At present, Britain is committed to take 232 of these planes at a price of £35m each. This will probably be scaled back to 184. But, according to Paul Beaver, a defence committee adviser and former analyst for Jane's, a publisher of defence information, just 84 would be ample. Similarly, while the job-creation scheme otherwise known as the Royal Air Force is braced to lose about 7,000 people, independent analysts reckon that 14,000 could go without any reduction in effectiveness.

The trendiness is apparent in the fashionable obsession with American theories that may not be easy to adapt to British circumstances. The Americans have themselves suffered in Iraq through their over-reliance on technology and firepower at the expense of other important capabilities, such as good intelligence, cultural understanding and the number of troops needed to do the job. With severely limited resources, British forces may end up not getting American-style firepower, while losing sight of their strength.

The army is already stretched to breaking point by the demands that Mr Blair has made of it. It needs to be better equipped, but above all, it needs more deployable manpower. Unless bigger savings are found elsewhere, the expense of aping American technology could mean that, in future, there are even fewer army boots on the ground than now.

Britain's armed forces shouldn't be a little echo of America's. What they do better than anybody else is the roughest end of peace enforcement. As the defence committee says: “There is still no substitute for numbers. We believe that true effect is a product of quality and scale.” It's a point that Mr Blair might wish to raise with Mr Hoon.

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Yukos

Cinderella's witching hour

Jul 8th 2004 | MOSCOW
From The Economist print edition

AP

Does Russia's Yukos face bankruptcy or break-up?

Get article background

AT MIDNIGHT on July 7th, Yukos's golden carriage began to turn into a pumpkin. As *The Economist* went to press, officials were waiting nervously at the oil firm's Moscow headquarters for bailiffs to turn up, brandishing not glass slippers but court orders allowing them to seize assets to cover the 99 billion rubles ($3.4 billion) that it has been ordered to pay in back taxes for the year 2000.

What broke Cinderella's spell? Once the belle of Russian business, wooed high and low by handsome investor princes, Yukos had still looked beautiful to many of them despite a year of unremitting tax and criminal probes. And two weeks ago it seemed close to a truce with the Kremlin. It had offered to sell its remaining stake in Sibneft—an oil company it bought last year—to pay off the tax bill. Viktor Gerashchenko, a former central-bank governor with good political connections, had become its chairman. President Vladimir Putin said that the authorities were “not interested in the bankruptcy of a company such as Yukos.” Investors believed him, and Yukos's shares shot up (see chart).

They are having doubts now. A tax official denied negotiations were going on; on June 29th, a court overturned Yukos's appeal against the tax claim. Two days later bailiffs arrived and gave Yukos until July 7th to pay. That same evening the tax ministry said it would sue for another 98 billion rubles for 2001. At the weekend prosecutors raided Yukos again. This week the chief prosecutor hinted at further tax claims for 2002 and 2003. Reports that Mikhail Khodorkovsky, Yukos's jailed main shareholder and ex-boss, had offered to give up his stake to cover the debt were denied by Yukos, confirmed by his lawyer and ignored by the authorities.

Creditors and minority investors got scared. A syndicate of banks led by Société Générale announced that Yukos was in technical default on a $1 billion loan, though they are not yet asking for the money. An investment fund, Roxwell Holdings, launched a lawsuit alleging that Yukos had misled investors.

And faith in Mr Putin's assurances began to fade. Though declaring Yukos bankrupt could take months, its

effective demise could come sooner. With its bank accounts frozen and oil-shipment fees due soon, it could have trouble doing business. Suppliers are already demanding money upfront. Its three main subsidiaries, which produce the oil and also hold most of Yukos's cash, could keep running for a while even with the parent company disabled, but not indefinitely: they have already cut investments to a bare minimum.

Investors have held their breath and wondered. Would the authorities accept Yukos's terms? Would they keep squeezing until Yukos agreed to theirs, whatever those are? Or would bailiffs start selling off the firm's subsidiaries to cover its debts? And if so, would they do it transparently to the highest bidder—maybe even a foreigner—or in a hasty fashion to state firms and others in the Kremlin's favour? And, again that question: what went wrong?

It has long been clear that the case was politically driven. The rigged auction by which Yukos was acquired, with the then government's blessing, was little different from others in the wild days of the early 1990s. And when it came to using tax havens, which the government began to abolish only last year, Yukos was not even the most effective (that distinction, according to Troika Dialog, an investment bank, went to Sibneft).

Theories abound about why Yukos became the Kremlin's target. But a mixture of hints and historical piecing-together suggest that Mr Khodorkovsky had done more than any other “oligarch” to defy Mr Putin's command that such people stop wielding political clout as they had during Boris Yeltsin's presidency. In particular, Mr Khodorkovsky's success in lobbying Russia's legislators to block the closing of tax loopholes persuaded the Kremlin that he—and by example, the others—needed to be taught a lesson.

Platon Lebedev, one of Mr Khodorkovsky's main partners, was arrested, and probes into Yukos were launched. Then Mr Khodorkovsky was thrown in jail on charges of tax evasion and embezzlement that could leave him there for ten years. Until recently, most assumed that the Kremlin would persuade or force Menatep, the firm that represents Yukos's main shareholders, to let go of Yukos while leaving Yukos itself relatively unharmed.

Instead, things have escalated. Perhaps there was never a deal in the works. Or perhaps, after Mr Putin's reassurances last month, Menatep became stubborn again. Or perhaps the process has acquired its own momentum. The conflicting signals coming from the government suggest either that only the very highest levels are privy to any talks going on, or that Mr Putin is not in full control of his underlings.

That is unnerving for both foreign and Russian business. An investigation of 140 other privatisations released this week by the audit chamber found irregularities in 56 of them, estimated to have cost the state $1.5 billion: small change next to the sums being demanded from Yukos, but enough of an excuse to make life difficult for many others. Even foreign oil companies, which are accustomed to unpleasant regimes, are playing it cautious. This week the government claimed that ChevronTexaco had plans to invest up to $10 billion in Russia, but the American oil giant, already burned this year by the annulment of an agreement to let it develop oil fields off Sakhalin Island, pointedly remarked that its investment decisions were led by “such factors as... the sanctity of contract conditions”.

A deal over Yukos's future may yet emerge. Yukos officials are defiant, saying that, if the idea is to strip out the subsidiaries and leave an empty shell, their complex ownership structure will make it a tough legal battle. But the authorities have already shown little regard for the niceties of the law. And if Yukos is picked apart and the spoils divided among its ugly sisters, handsome princes will steer clear of courting in Russia for a while.

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Rupert Murdoch

Global TV

Jul 8th 2004
From The Economist print edition

How DirecTV fits into News Corporation's media empire

EVER since Rupert Murdoch's News Corporation won control last December of DirecTV, America's biggest provider of satellite television, his rivals have wondered what he will do with it. DirecTV gives News Corp a national distribution system to add to its broadcast network, studios, television stations and cable networks. No other media conglomerate owns such a powerful arsenal. Best of all for Mr Murdoch, it will be difficult for anyone else to achieve the same degree of vertical integration, since politicians in both of America's two big political parties oppose more consolidation in the media industry.

So what is Mr Murdoch up to? So far, DirecTV's bosses, Chase Carey and Mitch Stern, have concentrated on turning the firm's engineering-based culture into one that is customer-led, like most media firms. In April, DirecTV sold PanAmSat, which owned 24 satellites, for $4.3 billion. A sure sign that the media folk are having their way, says Stephen Blum, a consultant to the satellite industry, came when Mr Stern swapped offices because his old one was suspected of having bad *feng shui*.

DirecTV is poised for rapid growth. It has 12.6m customers in America now—just under 16% of the pay-TV market. Mr Murdoch wants 20m by the end of the decade. In May, the firm said that it had added 460,000 subscribers in the first quarter of 2004, a 67% jump over the same period last year. Many switched from cable, which has three-quarters of the pay-TV market.

Until now, cable has never faced serious competition. But it has quickly woken up to the threat from satellite, and from DirecTV in particular. The cable operators have spent around $70 billion improving their technology and some offer customers high-speed internet access in a bundle with TV and telephone services. Satellite firms cannot provide such packages. Cable can offer other unique services, such as video-on-demand.

The answer to cable's strengths, argues DirecTV, is the personal video recorder (PVR), a device which makes it easy for people to record plenty of episodes of their favourite programmes. They can also skip through ads. When hooked up to DirecTV, they can store a large selection of on-demand content, including films, sport and TV shows. They can also provide interactive services, such as customised electronic newspapers, additional camera angles for watching sporting events, and voting in programmes like “American Idol”, a reality show produced by Fox Entertainment, Mr Murdoch's main content business. The PVRs ability to avoid ads could endanger some of News Corporation's revenues, admits Mr Carey, but “you can't stop what people want.”

Above and beyond DirecTV's ability to trounce its competition, owning it brings News Corp leverage in other ways. As a rival media chief puts it, the satellite company is “a cudgel to wield in a war of media giants” because it can provide extra negotiating power in programming deals. America's media regulator has placed a condition on Mr Murdoch: for six years News Corp must submit to arbitration over price disputes and not yank its programming off rivals' cable systems. Nevertheless, News Corp still has plenty of ways to benefit. It could extract higher prices for Fox programming by implicitly threatening to use DirecTV to start a price war in a particular cable market, says Craig Moffett, an analyst at Sanford Bernstein.

Mr Murdoch hopes to merge DirecTV's business in Latin America, which has 1.5m subscribers, with his Sky satellite operation in the region, which has 1.7m subscribers. He is awaiting approval from regulators. Many expect him to unite DirecTV with BSkyB in Britain—and, eventually, with Star, his Asian operator, to form a single, global satellite-TV company. Consolidating the American and British satellite firms would be desirable, says a News Corp executive, but there has been no formal conversation about doing it, and nothing will happen until the parent company reincorporates from Australia to America,

which is due to take place later this year. Then Mr Murdoch's global reach could be just around the corner.

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Aviation

Opening the throttles

Jul 8th 2004
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Airbus boosts production in the race against Boeing

Get article background

WITH the Farnborough International air show opening in Britain on July 19th, the ritual dog-fight has already begun between the two companies which now enjoy a duopoly for large commercial jets carrying over 100 passengers. Last year, Europe's Airbus took the lead for the first time with more deliveries than America's Boeing. It looks set to maintain that position: Airbus has landed orders for 104 jets in the first six months of this year, compared with Boeing's 73. A reflection of Airbus's confidence is a recent bold statement by its parent, European Aeronautic Defence and Space (EADS), that after three years of belt-tightening, production will expand by a huge 25% next year.

Both manufacturers are desperate to grab the headlines at international shows with order announcements. This week Boeing announced ten more tentative orders for its new 7E7 mid-sized, long-range jet, from a pair of European charter companies. They join All Nippon Airways and Air New Zealand as launch customers, which means they should enjoy big discounts as Boeing tries to build credibility for its latest aircraft. Meanwhile, executives from Thai Airways have indicated that they could become only the fourth Asian customer for Airbus's massive new plane, the 555-seater double-decker A380. Its order book has stood at 129.

Philippe Camus, co-chief executive of EADS, says the company sees only the beginning of a recovery in commercial aviation. Yet EADS stunned analysts at an investor forum when it said it was planning to increase production in 2005 and 2006 from 307 aircraft this year to 385.

On the back of such performance, plus progress with defence orders such as those for the A400M military troop carrier, the share price of EADS has soared to a three-year peak. Rival Boeing's share price has also risen to its highest level in two years, helped by a big defence order from the US Navy worth $3.9 billion. That was a rare bit of good news for Boeing's defence business, which has been mired in scandal.

Boeing and Airbus can also draw comfort from signs of a revival in air travel. IATA, the international trade association for airlines, says that for the first time airlines are enjoying traffic levels above those of 2000, the last normal year before terrorism, the SARS epidemic, war in Iraq and economic worries delivered blow after blow to the industry. But higher passenger numbers are not translating into higher revenues-per-passenger, because of price wars and over-capacity. Some carriers are adding capacity on potentially lucrative routes, such as the North Atlantic, which depresses prices. And low-cost carriers are piling pressure on network airlines in America, Europe, Asia and South America.

With more than 600 aircraft ordered from both manufacturers, and the huge increases in the capacity of carriers (particularly in Europe, see article) there are suggestions that a bubble is in the making. Nick Cunningham, an analyst at Citigroup Smith Barney in London, worries that the aircraft makers are seeing a repeat of the telecoms-equipment boom of the late 1990s. He points out that the strength of the share prices of the two big aircraft manufacturers belies the weak underlying position of their customers. The world's airlines had been hoping to turn a small profit this year, after racking up cumulative losses of about $31 billion over the past three years. But an oil price stuck firmly in the vicinity of $40 has increased their fuel costs and dealt them yet another blow. This means that, despite more air travellers, the airline industry as a whole is likely to face a fourth consecutive year of losses.

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China's beauty business

Saving face

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In China, beauty really is all about business

TO SEE how much of a commercial, western-like mind lurks beneath the modern Chinese woman's eastern aesthetic, turn to the case of Yang Yuan. The 20-year-old model from Henan province is suing the organisers of a beauty contest in Beijing for disqualifying her after discovering that she had had extensive cosmetic surgery.

Ms Yang, a minor celebrity on the mainland, argues that the whole point of going under the knife—she spent 110,000 yuan ($13,280) on alterations to her nose, lips and teeth, and a facelift—was to improve her appearance to get more modelling work and win, er, beauty pageants. Hence she is asking for 50,000 yuan compensation, not least to recoup some of her outlay.

The Beijing court that heard the suit has yet to rule. But whatever it decides, Ms Yang's case shows how fading social controls and cultural traditions combined with rising urban incomes are fuelling a boom in China's beauty business. Demand for lipsticks, make-up and lotions, both from foreign makers such as Revlon and local brands like Yue-Sai (recently bought by France's L'Oréal), is growing rapidly. Life-style magazines are mushrooming, as are plastic-surgery clinics. Beauty contests, once banned as “spiritual pollution”, are increasingly popular—China even hosted the “Miss World” pageant last year. Beauty clinics give discounts to clients who let them publish “before” and “after” photos—which is how Ms Yang was rumbled. In May, a Beijing hospital offered “guinea pigs” the chance to win seven free operations to become the first “artificially handsome man”. The Chinese beauty industry is now worth $24 billion a year according to one government estimate.

So far, so American. But there is a difference. Most western women (aspiring actresses apart) make use of beauty products or undergo plastic surgery primarily to boost their self-esteem. In China, by contrast, an enhanced appearance—often to add an eyelid crease and build up the nose—is primarily viewed as a ticket to higher earnings. Surgery is a commercial investment, often funded with a loan. Hence the willingness of many Chinese women to risk being operated on by badly qualified surgeons and equally their willingness to sue when things go wrong: official statistics reveal more than 200,000 malpractice suits over the past ten years.

But there is a happy ending in sight for the country's growing number of “man-made” beauties. A local businessman is planning an “artificial beauty” pageant in August, specifically for those who have had plastic surgery.

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Starbucks in Germany

Latte developer

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Karstadt's coffee loses flavour

HOW can a brand like Starbucks, in a coffee-drinking country like Germany—consumption: 158 litres (35 gallons) per-person per-year—fail to make money? After two years, KarstadtCoffee, which operates 31 Starbucks coffee houses at prime sites in 11 German cities, is still three years away from breaking even, according to its forecasts.

The answer may not be in the concept itself—iced caramel macchiato crosses the counter as briskly in Cologne as it does in London or New York—but in the deal that KarstadtQuelle, the German department store and tourism group, cut with Seattle-based Starbucks. Karstadt owns 82% of the joint-venture, with the remainder held by Starbucks. The deal means that Karstadt bears most of the investment costs. Both parties are coy about the details, but the arrangement does not seem to be giving KarstadtCoffee the 9% return on sales that it predicted so boldly when it signed up to the deal in 2001. There was talk of opening 200 shops by 2006. Now the planned total is 43 by the end of the year, rising to 180 by the end of 2007.

That is assuming Karstadt stays in the game. Wolfgang Urban, the boss of KarstadtQuelle, reportedly agreed to the deal during a game of golf (of which he is very fond) in Seattle with Howard Schultz, the chairman of Starbucks. Mr Urban was replaced on June 1st by Christoph Achenbach. Mr Achenbach, and Thomas Middelhof—the former chief of Bertelsmann, a German media giant, and head of Karstadt's supervisory board since July 1st—are now reviewing group operations from top to bottom. Savings and job cuts are widely expected, not least because most of its divisions made a loss in the first quarter.

But getting out of coffee might prove more expensive than staying in. According to some reports, KarstadtQuelle can sell its stake only to Starbucks—and for as little as 10% of the investment costs. Bon appétit Group of Switzerland was “bought out” by Starbucks in March 2003 from joint-ventures on terms that did not cover the investment costs. One reason given for making the Starbucks deal was that it could help revamp the group's staid department-store image. As that still has to happen, Karstadt may just have to brace itself with a double espresso and let its profligacy continue for a while longer.

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Mobile telecoms

The virtues of being virtual

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New brands of mobile-phone services are suddenly all the rage

Get article background

VIRGIN does it. 7-Eleven, Tesco and MTV do it. And Time Warner Cable, Wal-Mart and Disney are considering it too: offering mobile-phone services. Surely that means building an expensive network? Far from it. Instead, newcomers can simply form a partnership with an existing mobile-network operator, piggyback on their network and resell their service under their own brand. Becoming a "mobile virtual network operator" (MVNO) is an idea that has been around for a few years—but it now seems to be all the rage. Virgin, for one, has just announced plans to cash in on the mania by seeking a stockmarket listing for its British MVNO operation, Virgin Mobile, which has 4m subscribers. Why has the idea suddenly become so popular?

There are several reasons. For a start, says Kerry Ritz of Great River, a wireless strategy consultancy, network operators have finally overcome their ambivalence towards the idea of MVNOs. They have realised that it is always better to wholesale spare network capacity than to leave it unused. Better still, they have also noticed that MVNOs can help them capture customers in segments where their existing brands do not reach.

Virgin Mobile, which apart from Britain also operates in America and Australia, is aimed specifically at teenagers. Other virtual operators appeal to ethnic minorities. TracFone, for example, an American MVNO owned by America Movil of Mexico, targets the Hispanic community. Since its launch in 1996 it has signed up over 2m subscribers. Similarly, DBS Communications, another American MVNO, is doing well by appealing to urban blacks. Several overseas operators are now thinking of establishing MVNOs within America aimed at specific ethnic groups, says Daniel Torras, an analyst at Pyramid Research. A Chinese operator might, for example, launch one aimed at Chinese Americans, and offer low rates to call China as well as customer service in Chinese.

Interest in MVNOs is also being driven by the arrival of "third-generation" (3G) mobile networks, which are finally being switched on around the world. Operators that have built expensive 3G networks want to fill them with traffic as quickly as possible to recoup their costs. The original plan was that 3G's extra capacity would be used for whizzy high-speed data services such as video, but such services have not proved popular. Allowing MVNOs to resell airtime is another way for operators to fill their empty 3G networks.

Finally, regulators in some countries, notably Denmark, have forced operators to open their networks to MVNOs in order to boost competition. In Hong Kong and Ireland operators were allowed to build 3G networks only if they promised to share their networks with MVNOs, notes Carrie Pawsey of Ovum, a consultancy. France's telecoms regulator is also pushing for MVNOs to be allowed into the market. But in most countries such action is unnecessary, says David Lewin of Ovum, since operators are striking deals with MVNOs without being forced to do so by regulators. Operators and MVNOs have a symbiotic relationship, he says, and both now recognise the benefits of co-operation.

So which firms are best placed to transform themselves into MVNOs? Retailers are one obvious example, since they have strong brands and a network of stores through which to distribute handsets and sell airtime, often in the form of top-up cards. In other words, they have everything they need to become a mobile operator except a mobile network, which is why Tesco and 7-Eleven became MVNOs.

Another category of MVNOs is, curiously, telecoms firms—those that do not own their own wireless networks, that is. Britain's incumbent operator, BT, spun off its wireless arm, which has since been renamed mmO2, and now offers wireless service as an MVNO instead. Similarly, in America, AT&T spun off its wireless arm, which is in the process of being taken over by Cingular. Once the transaction is complete, the AT&T Wireless brand will revert to AT&T, and it plans to relaunch as an MVNO by reselling airtime on Sprint's wireless network. Becoming an MVNO would allow Time Warner Cable, a cable-television operator, to offer wireless service as part of its bundle of services.

Mickey Mouse mobiles?

Big media brands, such as Disney, are also logical candidates to become MVNOs. The latest phones support music, graphics and video, which ought to play to content owners' strengths, particularly since traditional network operators are struggling to become more content-savvy. Another consideration, says Andrew Cole, an analyst at A.T. Kearney, is that “wireless will be the next broadcast medium”. The ability to watch television on mobile phones is just around the corner, and will be available in Japan and South Korea, the world's most advanced mobile-phone markets, later this year. “So media companies have to get into mobile,” says Mr Cole.

Yet another possibility, notes Mr Ritz, is to use MVNOs as a form of marketing. Fashion brands, consumer-goods companies or record companies might become MVNOs. Having established direct links with their customers, they could offer them special offers or exclusive deals.

A less obvious category of potential MVNOs are low-cost airlines. Ryanair and easyJet, two European low-cost airlines, have both announced plans to launch MVNOs in Britain: Stelios Haj-Ioannou, easyJet's founder, will reveal his plans later this month. Mr Haj-Ioannou says the best MVNO business model is that followed by Telmore, a Danish firm. Subscribers sign up on the web and are sent subscriber-identity (SIM) cards in the post, which they slot into their existing handsets to make cheap calls. Sales, customer care and billing are all done on the web to cut costs, as with low-cost airlines.

Is there a limit to the potential for MVNOs? Yes, because mobile markets are already saturated in most of the developed world, so the number of MVNOs being launched seems unsustainable: there are only so many potential subscribers. Already, Virgin Mobile has pulled out of Singapore, and the attempt by Shell, an oil company, to offer an MVNO in Hong Kong aimed at motorists also fell flat. “For every MVNO that succeeds there will two or three that will fail,” says Mr Torras. The firms most likely to succeed as MVNOs, he says, will be those with strong brands, premium content, and an existing and loyal customer base. Anyone for *The Economist*-branded mobile phones?

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Texting

Je ne texte rien

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Why do the French send fewer text messages than other Europeans?

THOUGH they disagree about many things, there is one respect in which France and America stand shoulder to shoulder: neither country is terribly keen on mobile-phone text messages. In most parts of the world, zapping tiny messages from one handset to another is *de rigueur*. Over half a trillion such messages are sent every year, bringing in around $50 billion in revenues for mobile operators. Globally, the average number of messages sent per subscriber per month is around 35, though it is far higher in some countries. But in France and America, texting has proven much less popular (see chart). Why?

America's lack of enthusiasm is relatively easy to explain. Several different and incompatible wireless technologies are in use, and the necessary plumbing to enable texting has only recently been put in place. Furthermore, voice calls on mobile phones are cheaper than in other countries, which gives cost-conscious users less incentive to send texts instead. And texting is often an additional service that must be paid for and switched on, so customers cannot be sure that a message to a friend will get through. This is not the case in France, however, which uses the same mobile-phone technology (called GSM) as all other western European countries, where texting is hugely popular. So why is it not in France?

For a mixture of reasons, says Stéphanie Pittet, an analyst at Gartner, a research firm. For a start, the French mobile-telecoms market is the least developed in western Europe: only around 65% of the population has a mobile phone, compared with around 90% in Britain, Spain and Italy. The usual explanation for this is a desire to protect Orange, the dominant mobile operator, from too much competition. Orange is part of France Telecom, which is partly state-owned, has huge debts and relies on Orange's revenues to prop it up. Less competition means higher prices and fewer of the cost-conscious, late-adopting subscribers who tend to like texting.

Another factor, says Jessica Sandin of Baskerville, a firm of telecoms analysts, is that French operators were late to introduce texting and slow to interconnect their networks to allow subscribers to text each other and those in other countries. Prices have now been cut to make texting more attractive. But it does not seem to be helping. “At this point they should be catching up, but they aren't,” says Ms Sandin.

So it is difficult to avoid the conclusion that cultural factors also play a role: perhaps mobile phones simply do not fit in with the relaxed French lifestyle, with its short working week and unusual respect for traditional ways of doing things. But perhaps even that is being too kind. “I think they are just technophobes,” says Ms Pittet, somewhat ruefully, of her compatriots.

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Face value

Private money and family fortunes

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Stefan Messer used private equity to regain control of the family firm

OFTEN the story goes like this: bankers and private-equity investors find a family firm, persuade the owners to sell, pay them cash, load up the balance sheet with debt, cut costs, strip assets and then sell what is left to a rival company. Stefan Messer's story provides a cheerful variation on the theme.

Mr Messer is the grandson of the man who founded Messer, once one of the world's biggest producers of industrial gases. He invited Goldman Sachs, an investment bank, and Allianz Capital Partners, a private-equity firm, to help him rescue his company from an almost certain break-up or merger with a competitor. The result is that, 39 years after his father Hans sold two-thirds of his firm to Hoechst, a German chemicals giant, a Messer is back in charge of the family firm.

The company is, though, only about a third as big as it once was. But its best assets are now in parts of the world that promise rapid growth: central Europe and China. Mr Messer is happy, even though he spends most of his time visiting his far-flung domain. “This business is my life,” he says. Retiring with the loot from the sale of his stake at the age of 49 was not an option he would consider.

The spark of change

The company has changed before to meet new growth opportunities. In the early 1900s Adolf Messer, the founder, quickly moved from gas lamps, suspecting that electricity would do the job better, to making welding equipment and industrial gases. Based near Frankfurt, the firm survived two world wars, including a 1944 bombing raid. Hans took over in 1953 aged 28. The company then expanded into other parts of Europe and into Mexico. In 1965, Hans merged the company with Knapsack-Griesheim, a subsidiary of Hoechst. Hoechst had 67%, but the Messer family kept 50% of the voting rights. Messer Griesheim was run at arm's length. When Hans retired in 1994, a new chief executive drafted in from Hoechst embarked on rapid expansion into North and South America, South Africa, central Europe and Asia. In theory Stefan Messer and his family could have vetoed what they feared was an extravagance, but they relied on the judgment of Helmut Maucher, the head of Nestlé, and Carl-Ludwig von Boehm-Bezing, a board member of Deutsche Bank, who represented their interests on the supervisory board and the shareholder committee. “I was young and inexperienced,” recalls Mr Messer, “that was my mistake.”

In 1997, Hoechst decided to focus on life sciences and started to lose interest in Messer Griesheim. Mr Messer, who was running the company's French subsidiary, knew a spin-off was only a matter of time and thought that the family stake would be diluted. In 1999, when Hoechst merged with Rhone-Poulenc to form Aventis, it decided to sell Messer Griesheim's welding business. Mr Messer invited Carlyle, a private-equity firm, to join him in a successful buy-out of this part of the business. “You could say that was a test run for what happened later,” says Hans-Gerd Wienands, a partner of Freshfields Bruckhaus Deringer, a law firm, and a close adviser of Mr Messer.

Later, talks began with Linde, Messer Griesheim's biggest German competitor, about merging the two companies. But Linde feared that it would face antitrust problems and bought Aga of Sweden instead. Stefan Messer decided it was time to try the private-equity route again, but this time to take control of the entire company. Alex Dibelius, co-head of Goldman Sachs in Germany, and an adviser to the Messer

family, initiated talks with Paul Achleitner, his former Goldman boss, who was now a board member at Allianz. In 2001 the private-equity arms of Allianz and Goldman Sachs, assisted by Goldman's investment bankers, constructed a deal which bought out Hoechst and put them in as 67% shareholders. They financed it with a *euro*550m ($493m) ten-year bond, but one paying a high rate of interest. Mr Messer, with an eye to the future, insisted on an option to buy the company outright after three years, although most people thought that a trade sale or even a stockmarket flotation was more likely.

But Mr Messer was determined to gain control. Last year he began to discuss selling large chunks of the company to finance a family purchase of the bits he wanted. He was excited most by two regions: central Europe and China. In the end, operations in Germany, North America and Britain were sold to Air Liquide, to make it the biggest industrial-gas producer in Europe. Although Mr Messer sacrificed shares in an empire that stretched from Lima to Kuala Lumpur, he is now chief executive of a smaller, but still far-reaching domain, and one he can control himself. This month, banks are putting the finishing touches to a *euro*525m loan to finance the business, and at more beneficial rates than the bond used to buy out Hoechst.

In the industrial-gas business small players have as much chance as the giants in grasping big opportunities, Mr Messer argues. This is because of transport constraints. Oxygen, for instance, is carried in tanks in liquid form or compressed in heavy cylinders, and sometimes distributed through pipelines in places where steel or chemical plants are concentrated. The maximum effective transport radius is 300 kilometres (186 miles). This leaves plenty of scope in China and Europe to win market share region by region. Messer is already in four industrial regions of China, serving mainly steel complexes, and is now eyeing inland provinces. It also has a foothold in most countries of central and eastern Europe: it went early into Bosnia, Croatia and Serbia. Meanwhile Goldman Sachs and Allianz Capital would love it to be known, from this example, that although they might have made more money if they had found an industrial buyer, they can be fairy godmothers to family firms who might be wary of using private equity.

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Low-cost airlines

Turbulent skies

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Getty Images

Innovative and bold low-cost carriers have transformed the airline industry on both sides of the Atlantic. But are they now doomed to lose their momentum?

Get article background

EVER since its creation nearly a century ago, the commercial-airline industry has been prone to abrupt ups and downs. Changing aircraft technology, big capital investments and the shifting priorities of governments have repeatedly forced airline operators to scramble to stay aloft. Yet few of these periods of change have promised to transform air travel as thoroughly as the wave of increased competition, new entrants and aggressive price cutting now sweeping through the airline business in both Europe and America. A slew of new low-cost airlines is attacking big incumbent network carriers, some of whom will probably not survive. What shape the industry will take after this shake-out remains unclear, but one thing seems certain: passengers are already being offered more choice and better prices.

When low-cost airlines were first launched in Europe after the liberalisation of Europe's domestic airline market was completed in 1997, Ryanair and easyJet, the pioneers, explicitly and expertly mimicked American budget airlines such as Southwest and ValuJet (now AirTran). The essential elements of the business model were: a single-type fleet of planes; fast turn-rounds; use of cheap secondary airports; no frills—definitely no moisturiser in the toilets; and enticingly low fares that rose only as a flight filled up.

But today the American and European budget-airline sectors have somewhat diverged. Partly this reflects the relative maturity of the concept in America and its youth in Europe. But intriguingly, the differences go deeper than that. America's budget airlines are starting to move upmarket in service quality, whereas Europe's give every impression of moving relentlessly downmarket. They emphasise dirt-cheap tickets, yet they are also expanding as they try to fend off start-up competitors. At the same time, both of Europe's leading low-cost airlines have blurred the simplicity of the original business model they adopted from their American predecessors.

A generation after deregulation of America's airlines in 1978, low-cost carriers have seized control of the domestic market. It was not always thus. Of the 34 newcomers created after deregulation, 32 soon went bust. Those were the days when the strong, incumbent firms such as American Airlines could simply unleash even lower fares whenever a low-cost upstart invaded its market. Before the antitrust authorities could do anything about it, the competitor was crushed.

Low-cost airlines may now be mature as a concept in America, but the market remains in flux. Since September 11th 2001, the six largest network carriers have slashed costs and reduced capacity by one-

fifth as they have struggled to stay financially solvent. Even before the terrorist attacks, however, budget airlines were on a roll. Since 2000 they have expanded capacity by 44%. Low-cost carriers currently have 400 orders out for new planes, whereas the old network carriers have only 150 planes on order.

Most of the expansion has come from JetBlue, Frontier and AirTran; Southwest, which accounts for nearly half the sector, has been obliged by the wider air-travel recession to check its expansion, although it is now returning to its former growth path of 10% a year. Southwest is the fourth-largest American airline by passenger numbers, and so was bound to suffer more than younger budget carriers.

Behind the current recovery there lies a bitter truth for network carriers. Though their passenger numbers are rising, revenues remain flat because they cannot raise prices. As the cost of jet fuel soared in the spring, some network carriers tried to compensate by raising ticket prices, only to give up within days. Budget airlines control pricing in the market.

The cost advantages enjoyed by low-cost carriers are striking. Flexible workforces mean that airlines such as Southwest need only 80 workers to fly and support each aircraft, compared with 115 or more at a traditional network carrier. For passengers, the clearest evidence of the rival cost structures is the way the cabin staff of low-cost carriers parade rubbish bags before and after each landing, performing the task assigned by the network carriers to an expensive, standby cleaning crew.

Some big carriers have tried to mimic the low-cost airlines' business model. Song and Ted are owned respectively by Delta Air Lines and United Airlines. Even Hooters, a chain of restaurants that features buxom waitresses, has joined the fray with a niche airline of the same name. And yet until recently, there had only been one highly successful low-cost start-up, JetBlue. That is now changing.

Last month Independence Air was relaunched, having transformed itself from Atlantic Coast Airlines, which had previously run sub-contracted feeder services for United. Sir Richard Branson, a British entrepreneur, then formally announced the launch next year of Virgin America. His Virgin group will own half the airline. American private-equity investors will own the rest (federal law restricts foreigners to owning no more than 49% of the economic equity and 24.9% of the voting shares in any American carrier).

The business model for low-cost carriers is becoming increasingly varied. Song and Ted are following in the flight path of failed network-carrier offshoots in the past, such as Shuttle by United (beaten by Southwest in the west-coast market in the 1990s) and Continental Lite. Song's debut is still dogged by the ongoing labour and financial problems of its parent, while Ted is a highly specialised airline running mainly on holiday routes from United's hubs, such as Chicago.

A nice, cheap package

Meanwhile, the transformation of charter airlines (which run flights tied exclusively to holiday packages) into leisure-market low-cost scheduled carriers is mirroring what has been happening to charter airlines in Europe. The traditional market for package holidays has been undermined by the sheer variety of destinations now served by low-cost carriers and by customers' ability to book accommodation over the internet. People can create their own packages now. In Europe, 99% of low-cost booking are made through the internet, compared with 75% in America.

Another category of low-cost carrier in America is the regional airline that has converted itself, often while also extending its range: Frontier and America West are the best examples. A result is that few local or regional markets are now free of a low-cost competitor. It is estimated that low-cost competition exists on 70% of American routes. Low-cost carriers have seen their market share in recent years grow to around 30% nationally. Competition is thus increasingly between the low-cost carriers themselves.

In response, leading budget airlines have altered their image. Southwest and JetBlue have developed strong brands, offering a well-defined service rather than just low prices. They are attracting business passengers, and sometimes they even offer a separate business cabin. The emphasis at JetBlue is on slick and stylish service and an enviable punctuality record.

But the bigger these carriers grow, and the more they offer such features, the less distinguishable they become from network carriers. Southwest's coverage of the nation is now so complete that 20% of its passengers actually make transfers between its own flights, while at JetBlue 10% similarly transfer. Imagine watching a time-exposure photograph that shows a budget carrier transforming itself into a kind

of network carrier, albeit one inherently leaner and more economical.

Another clue as to how America's low-cost carriers are evolving comes from the role played by hub airports. Once anathema to the budget airlines, and the major feature of their network rivals, hubs have increasingly become part of the business model for some low-cost carriers as well. AirTran and Frontier run what amount to hub-based services out of their respective bases in Atlanta and Denver. The deeper the low-cost carriers have delved into out-of-the-way point-to-point routes, the more they are starting to find themselves developing hubs—albeit of a sort.

For instance, JetBlue is now buying 100-seater regional jets from Embraer, a Brazilian manufacturer, to add to its fleet of Airbus A320s. This will enable it to run new routes to smaller markets and to add flights on routes to bigger ones. But the combination of small and larger jets could lead to a situation in which JetBlue is feeding traffic into bigger airports, then transferring passengers to its Airbuses from the little regional jets.

The most radical approach has been adopted by Independence Air, a new low-cost carrier operating from Washington's Dulles airport. From September it will have 300 daily flights to 35 destinations, with more services to follow. But this is a new kind of low-cost carrier, operating from one hub, rather than a string of point-to-point routes across the country. Despite scepticism in the industry, some think the airline is so focused that it can succeed.

But perhaps the biggest change in the business model is that some of America's low-cost carriers are moving upmarket. In the process they clash with the beleaguered network carriers (never very customer-friendly at the best of times) moving downmarket as they desperately seek to cut costs. For some years, in-flight food on a domestic network-carrier has been a shrink-wrapped disaster lobbed from several rows away by a sullen and stressed cabin attendant. Low-cost airlines such as Southwest and JetBlue have studiously avoided the problem: where they do offer food, it is with style and smiles.

Nevertheless, the headlong growth of America's low-cost carriers will almost inevitably face problems. Southwest has excellent labour relations and a cheery, family-style culture, reinforced by lots of company events. But recently its cabin attendants have been seeking new contracts that, if granted, would include some of the conditions that their counterparts enjoy on network carriers.

What would happen if these employees start to take a bigger slice of the corporate cake? The sheer pace of the low-cost sector's expansion is enough to induce vertigo. JetBlue, for instance, doubled in 2002, grew by 66% last year and will grow by around one-third this year. AirTran has also been growing at more than 20% in successive years. It cannot last.

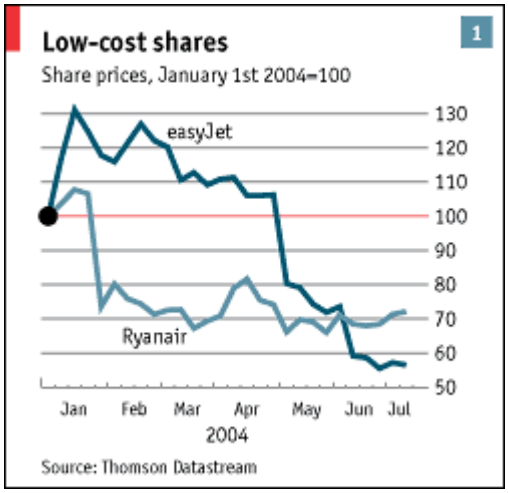
Europe's turmoil

The biggest difference between low-cost carriers in America and Europe is that they have existed in Europe for less than ten years. No surprise then: Europe is in the shake-out phase. Loads of new carriers have sprung up. But most of these will disappear rapidly, just as their American equivalents did. The splurge of new carriers explains the over-capacity, but not the price war that is going on in Europe. Intense competition is taking its toll not just among the doomed newcomers, but on the industry leaders as well.

The shares of Europe's two leading budget airlines, Ryanair and easyJet, have fallen steeply in recent months, after both companies issued profit warnings (see chart 1). Michael O'Leary, Ryanair's vocal and aggressive boss, has warned of a “bloodbath” in the low-cost market. Both he and the bosses of easyJet have complained about crazy pricing by start-up budget carriers that have no hope of surviving. EasyJet confirmed this week that one option its founder and biggest shareholder, Stelios Haji-Ioannou, might consider is to take the group private with the aid of a private-equity investor.

The trouble is that the low-cost-carrier sector in Europe faces serious challenges. At present an all-out war rages between airlines in general. Europe has around 50 low-cost carriers, although that total changes from week to week as new ones are

launched and others go bust. Low interest rates, a glut of second-hand airplanes, off-the-shelf software and the example of the successful market leaders have lured others into the market.



Another factor has been this year's expansion of the European Union to include ten more countries. In joining the EU, these countries also joined its deregulated domestic aviation market, giving entrepreneurs their first chance to fly in and out of them. As a bonus, the market leaders have so far shown remarkably little interest in central Europe. But they have responded to competition with their own crazy fares—off-peak return flights from London to Rome or Malaga are sometimes less than the £10 ($18) airport tax levied in London.

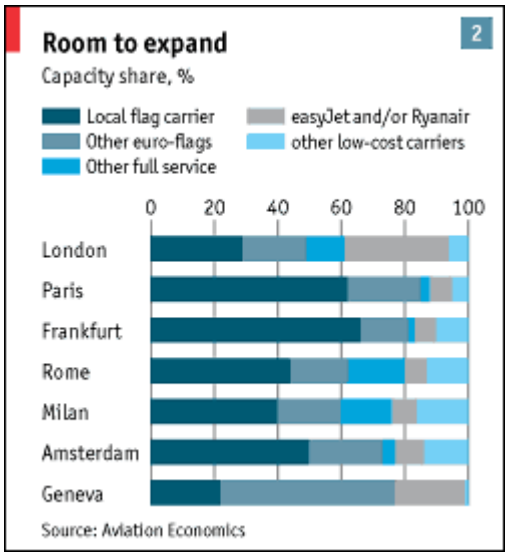
Nor is the war entirely among low-cost carriers. Network carriers such as bmi and British Airways (as well as one formerly stodgy flag carrier, Aer Lingus, that has re-made itself as a sort of low-cost carrier), have successfully adopted the internet-selling and yield-management techniques of low-cost rivals. They are not always as cheap as the likes of easyJet and Ryanair, but often at busy periods their fares to holiday resorts compare well. The traditional airlines also offer business travellers a wider range of flights to helpful destinations at prices from London Heathrow that are competitive with low-cost carriers flying from London's more distant airports, Stansted and Luton.

There is, however, something slightly disingenuous about Ryanair and easyJet moaning about over-capacity. Both carriers have ordered huge quantities of aircraft, tempted by fantastically low prices offered by Boeing and Airbus when orders were scarce. Ryanair has about 100 Boeing 737s on order, while easyJet has ordered 107 A319s from Airbus.

Keith McMullan of Aviation Economics, a London consultancy, has calculated that each of these aircraft would have to carry 250,000 passengers a year to earn their keep. In 2003 easyJet carried 21.1m passengers, while in the year ending in March 2004 Ryanair carried 23.1m. In order to fill up all the new planes, already arriving in their fleets at the rate of one every fortnight from now until the end of 2008, Ryanair and easyJet will need between them to attract 52m new passengers a year, more than double their current numbers.

Finding those extra passengers could prove difficult for two reasons. The first is that the current pattern of low-cost carrier traffic in Europe is essentially a British/Irish phenomenon. Ryanair first expanded by flying Irish expatriates and their kin between England and Ireland. This is what airlines called "VFR" (visiting friends and relatives) traffic. Much of it widens the market to people who had never flown before, or did so very seldom because of the high cost of tickets. But VFR travel is much more prevalent in a big homogeneous market such as America than in a fragmented one such as Europe.

Chart 2 shows the obstacles to low-cost carriers expanding across Europe. The comparison illustrates how the London airports are dominated by low-cost traffic, with the sector's share at almost 40%, against only 12% in Paris and less than 20% in Frankfurt's airports. EasyJet and Ryanair have a measly 7% of intra-European flights at Paris Charles de Gaulle, Orly and Beauvais combined. EasyJet has complained about discrimination at Charles de Gaulle, where it pays the same landing fees as Air France, but is relegated to Terminal Three, a bus ride away from the main airport.



Ray Webster, easyJet's chief executive, is also trying to challenge the way slots are allocated at Orly, the second Paris airport. He contracted to buy his Airbuses around the time that Air Lib, a failed French carrier, was going under, and he assumed that he could pick up many of its landing slots. Indeed, some sources suggest the collapse of Air Lib was a condition in the Airbus contract. But when that duly came about, French airport officials handed most of the slots to Air France. Mr Webster's message to the French government for the past year or so has been blunt: "We bought your bloody aircraft, now give us somewhere to land them."

New routes wanted

Most of the bases operated by easyJet and Ryanair are in Ireland or Britain. Unless they can gain greater access to airports in France and Germany (where they are making some progress) and so tap new markets, both will struggle to maintain their growth. It is not much use having open skies without open airports. To cope with this impasse, Mr McMullan suggests that the leading pair will have to continue their bitter price war against upstarts.

Other strategies that dilute the purity of the original American model have already been tried, with the takeover of Buzz by Ryanair and of Go by easyJet; easyJet's use of London Gatwick as a base; and Ryanair's decision to fly to Rome's Ciampino airport despite the expense. Perhaps it is also time for them to consider joint-ventures with local airlines of the kind successfully undertaken in Asia by Tony Fernandes of AirAsia.

Bosses of Europe's leading low-cost carriers are also still trying to customise their formats. Ryanair, for instance, is considering two initiatives that would differentiate its service. At the same time as it is stopping its seats from reclining (fixed seats are cheaper and need less maintenance) it might also equip the seats with high-tech backs that allow customers with credit cards to watch movies or gamble during their journey (an upmarket move?). And, more ambitiously, it might try to slash costs again, perhaps by making planes more like trains and allowing only cabin baggage (seriously downmarket).

Whatever strategies the budget airlines choose, it is clear that the original business model is evolving on both sides of the Atlantic. As they move upmarket in America to fill the void left by big network carriers, and as they move to more expensive airports in Europe, the risk is that low-cost carriers everywhere will start to acquire the very same high costs that made their network competitors so vulnerable.

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The dollar

Keep an eye on it

Jul 8th 2004
From The Economist print edition

After a buoyant start to the year, the dollar seems headed for a tumble

Get article background

THERE was a time, not long ago, when economists and those who dabble in the foreign-exchange market could find scarcely a good thing to say about the dollar. Last year, John Snow, America's treasury secretary, even managed to transform his country's long-standing strong-dollar policy into a weak-dollar one. All this greatly irritated Europeans, especially; as the euro rose, international meetings of the great and the good were dominated by cross discussions about the beleaguered buck. Newspapers, including this one, were full of gloomy headlines suggesting that the greenback would, indeed should, fall farther.

So it did, for a while: by early January, the dollar was worth a quarter less, in trade-weighted terms, than it had been two years before. But when everyone is betting that a market will go one way, it often goes the other. By mid-May, the dollar had risen by 8%, bucked up, as it were, by the Bank of Japan, which bought ¥14.8 trillion ($138 billion) of foreign exchange in the first quarter, almost all of it dollars, in comfortably the largest-ever act of intervention by a central bank. Then, quietly, the dollar started to drop. By July 6th, it had fallen by 4.3% from its high. Not surprisingly, perhaps: the dollar's prospects look even worse now than they did last year.

The dollar's recent decline may seem puzzling, for it began while expectations were mounting that the Federal Reserve was about to put up interest rates. The decline has continued since those expectations were confirmed on June 30th. Rising interest rates, you might have thought, would halt any such decline.

That is true only up to a point. As the American economy brought forth jobs in the spring, and the markets started to expect that the Fed would increase rates sooner rather than later, the dollar was boosted. A prime reason was that traders who had previously borrowed greenbacks in order to exchange them for other, higher-yielding currencies now needed to buy them back in a hurry. Lately, however, softer economic data have sown the idea that the Fed might not have to raise rates so far and fast after all. That has done the dollar no favours in recent days.

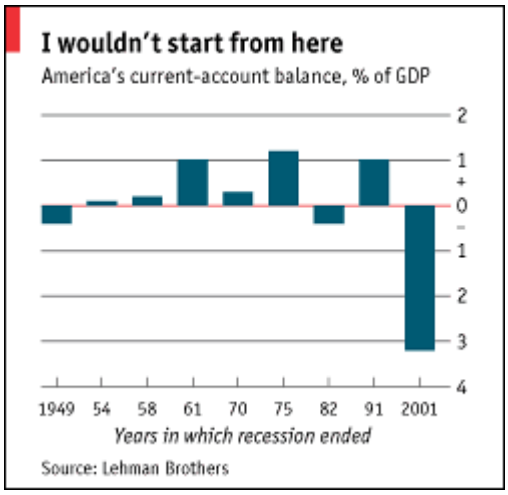
In the longer term, though, higher interest rates may be a curse for the dollar, not a blessing. To see why, look at that large and growing thing that goes under the name of America's current-account deficit. A country's current-account essentially comprises two things: the trade balance and net income from foreign investments. America runs a trade deficit that in April amounted to $48.3 billion, up from $46.6 billion in March. This alone implies an annual deficit pushing $600 billion, or 6% of GDP. The current-account deficit would be greater still if America did not make more money on its investments abroad than

foreigners earn in the United States.

That it makes a profit is odd, because it has net foreign liabilities (ie, the value of Americans' assets abroad is less than that of foreign claims on America). According to the Department of Commerce's Bureau of Economic Analysis, net liabilities amounted to 24% of GDP last year. America has an investment-income surplus because yields are much lower at home than abroad. All things equal, says Goldman Sachs, a yield of 6% on ten-year Treasuries would add 1% of GDP to the current-account deficit within a few years.

Economists fret about America's current-account deficit because it is a measure both of America's ability (or inability) to save and its attractiveness to foreign investors. The country's heady growth of recent years has relied on foreigners' willingness to invest there: Americans, in effect, spend other people's money. That need not matter when the sums are small, but it does when they are large and getting larger. Most economists believe that at some point the dollar will need to get cheaper, maybe much cheaper, to encourage foreigners to finance the deficit. That point may be at hand.

There are two weighty pieces of evidence to support this view. The first is that America started this latest recovery much deeper in hock to the rest of the world than it did previous ones, says John Llewellyn, the chief economist at Lehman Brothers. As the chart shows, America has usually started to pull out of recession with its current account roughly in balance. This time, it began with a deficit of 3.2% of GDP. Because growth tends to increase the deficit—America has sucked in imports and borrowed more—the deficit has widened. “I can easily imagine it going to 7% and beyond,” says Mr Llewellyn.



The second piece of evidence comes from investors' behaviour. Some say that the deficit is not a problem, but simply reflects foreigners' boundless desire to invest in a vibrant economy. This may have been true once, but not any more. Net foreign direct investment (FDI) was negative, to the tune of $155 billion, in the past 12 months, says Goldman Sachs. This ought to be no surprise: in the first quarter returns on FDI in America were 5.5%, while those on FDI abroad were 11.7%.

In recent years, the current-account deficit has instead been financed by (less stable) portfolio flows into stocks and bonds. In the past year, three-quarters of such investment in America has gone into bonds. The biggest buyers have been Asian central banks, trying to keep their currencies from rising too swiftly against the dollar (or maintaining a fixed rate, in China) and parking the money in Treasuries.

But this intervention has had a cost: inflation. Because the central banks bought the dollars with newly minted local currency, inflationary pressures have risen throughout Asia. This is fine for Japan, which has deflation, but not for its neighbours. Intervention thus seems to have stopped; even Japan turned off the tap in March. The central banks might, of course, wade back in if their currencies rose too much. But given the risk of inflation, it would be brave to bet on this. And if they do not buy the buck, who will?

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Financial regulation in Dubai

What odds now?

Jul 8th 2004
From The Economist print edition

Dubai is having problems with its new financial centre

THE ruler of Dubai, part of the federation of the United Arab Emirates (UAE), likes a sporting challenge. Sheikh Mohammed bin Rashid Al Maktoum's Godolphin racing stable (named after the legendary 18th-century Arabian racehorse) has landed 107 international race wins in ten years. Now he faces a tougher gamble close to home. Two years ago Dubai, as part of its slick diversification into service industries before its oil and gas run out, started creating a world-class financial centre.

Given its history—involving allegations of gold smuggling, money laundering and dodgy trading in nuclear gear from Pakistan—Sheikh Mohammed wisely hired world-class regulators. The Dubai Financial Services Authority (DFSA) was chaired by Ian Hay Davison, a veteran of the struggle to clean up Lloyd's insurance market in the 1980s, and Phillip Thorpe, formerly of London's Financial Services Authority.

Then suddenly last month Mr Thorpe was ejected from his office by security guards. Mr Hay Davison, on holiday in France, was fired by e-mail. They had objected to the board of the Dubai International Financial Centre allowing two of its members (in turn, members of the ruling family) to buy a couple of plots on the huge centre being built on the edge of Dubai City.

No one alleges wrongdoing, just poor corporate governance. When the two men put their concerns in writing last month, the centre fired them. The regulators were supposed to be independent, but the special decree establishing that had not been passed.

This left other members of the regulatory body's governing council, including such luminaries as Robert Clarke, formerly America's comptroller of the currency, and Robert Owen, chairman of the Hong Kong Securities and Futures Commission, in an embarrassing position. They sought an audience with Sheikh Mohammed at his country place west of London.

He promised their independence would be guaranteed; their new chairman Habib Al Mulla, a leading UAE lawyer, will report directly to him. Nothing like recent events would ever happen again. Now Dubai must persuade other international regulators to recognise the DFSA, and the 44 leading financial institutions thought to be interested (including Credit Suisse, Standard Chartered, Aon and Deutsche Bank) to join the trading centre when it opens “in a matter of weeks”. Quite a gamble.

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The BCCI case

Half-time in the High Court

Jul 8th 2004
From The Economist print edition

Depositors and the Bank of England are fighting a legal battle of attrition

IN SPORT, half-time gives weary athletes a welcome breather. For the protagonists in the London court case over the Bank of Credit and Commerce International (BCCI), which imploded under the weight of fraud in 1991, there is no such respite. This week lawyers for the plaintiff, Deloitte & Touche, liquidator of BCCI, were due to rest their case against the Bank of England, after the longest opening address in English legal history, lasting around 80 days. Before the Bank opens its defence in September, the two sides are due to tussle over a side-issue before the House of Lords, the country's highest court.

Deloitte accuses the Bank not of negligence (by law it is immune from such charges) but of “misfeasance in public office” for failing to regulate BCCI adequately in the decade or so before its collapse. BCCI's failure cost depositors more than $10 billion. In previous legal settlements, including those against BCCI's former auditor and the government of Abu Dhabi, Deloitte has recovered 75% of creditors' money. It is now seeking £850m ($1.5 billion) in damages from the central bank.

The case never promised to be swift and simple. Just getting to court took 11 years of squabbling between Deloitte and the Bank. The charge of misfeasance in public office is rarely used and hard to prove. Deloitte must show not merely that the Bank botched the regulation of BCCI, but that it did so in “bad faith”, knowing that its actions would harm depositors.

Deloitte has taken the judge through 60,000 pages of documents in order to buttress its charges. It says that the Bank licensed BCCI to do business in 1980 when it was clear that BCCI did not meet the proper criteria. It claims that the Bank then shirked its duty to oversee BCCI by claiming it was the job of authorities in Luxembourg, where BCCI was incorporated, despite evidence that its operational headquarters were in London and signs that the bank was wobbly. It also argues that Bank officials kept evidence of wrongdoing at BCCI from successive governors and deputy governors of the Bank, the Treasury and American investigators, and from Lord Bingham's inquiry into the bank's collapse in the early 1990s.

The paper mountain may grow higher still. Later this month the House of Lords will consider Deloitte's request that some documents exchanged in confidence between the Bank and its lawyers during the Bingham inquiry be released. An earlier dispute over document disclosure was decided in Deloitte's favour.

Neither side is about to give up. Deloitte has been working on its suit for a decade. For the Bank's part, someone close to the case says that admitting misfeasance is “tantamount to admitting that Bank officials were deliberately dishonest. It would be a disaster for its reputation.” Mervyn King, the current governor, wrote in the Bank's latest annual report that it was “impossible to contemplate settlement” and vowed the claim would be “vigorously defended”. Mr King also lamented the spiralling cost of the protracted court case: an estimated £21m this year to the Bank alone, almost 10% of its overall operating budget. With a long second half ahead, he had better get used to it.

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Banking jitters in Russia

There's always Sberbank

Jul 8th 2004
From The Economist print edition

Russia's biggest bank should benefit from depositors' nervousness

Reuters

Gutted about Guta

FOR what prides itself on being not only Russia's largest private bank but also its most advanced, with modernist branches and multifunctional cash machines, a run on deposits must have been a genuine indignity. On July 7th, Alfa Bank insisted for the third time in 48 hours that it was not running out of funds. It claimed that it was a victim of dirty public relations. Having survived the 1998 crisis that brought most other banks to grief, it is probably right; but many depositors (including our Moscow correspondent) took no chances.

Analysts are now waiting to see whether the liquidity crisis that has affected some smaller banks in the past two months will spread to the top 20. On July 6th, Guta Bank, a very visible Moscow outfit with $210m in retail deposits and 400,000 individual accounts, announced a suspension of payments. Guta is solvent, and with over $1 billion in assets it ranks roughly 20th among Russia's banks. Even so, its depositors—including companies affiliated with it in the Guta Group—withdrew $345m in June amid rumours that the authorities were investigating the bank.

A conspiracy theorist might think officials had gone out of their way to create trouble. In early July, Vneshtorgbank, a state-owned bank, announced that it had refused Guta a $400m credit. Guta then turned to the central bank, which also denied it help. According to Guta's chairman, however, the central bank is now quite willing to grant a loan to finance the acquisition of his institution by Vneshtorgbank—in effect, nationalisation. On July 7th, Guta's board approved the sale.

Regardless of what the authorities were up to, the jitters are exposing the weaknesses in Russian banks. Capital is again fleeing the country, interbank borrowing accounts for up to 20% of banks' liabilities and there are regulatory limits on the penalties banks can impose on term depositors who withdraw money early. Under such conditions, the central bank's recent moves to police the system have, say some analysts, created “a crisis of confidence”. Some banks have stopped lending to each other and depositors are fleeing. Owing to many banks' murky ownership and operations, depositors respond to any likely gossip, as do risk-assessment officers in the interbank market, says Dmitry Dmitriev, an analyst at United Financial Group.

The central bank has quickly halved its reserve requirements to 3.5%, about all it can do to boost liquidity, short of printing roubles. (Another option, lending to troubled banks, tends to provoke charges of favouritism.) Since Russian banks do such a bad job of supplying credit to the economy, most analysts do not expect their problems to spread to other industries.

Does anyone gain? Yes: a clear winner is Sberbank, of which the state owns over 60%. It is the only bank with a full state guarantee and Russia's only widely traded banking stock. It has 64% of retail deposits. Until recently it had been losing market share. But many observers now expect Russians to flock back, a desperate move because Sberbank imposes high transfer fees to prevent depositors leaving. Despite its bloated staff and a penchant for lending to corporations at curiously low rates, on July 7th several investment banks upgraded their recommendations on its shares. Among them: Alfa Bank.

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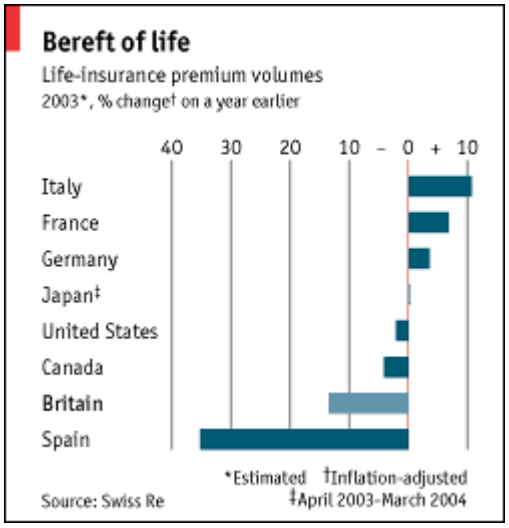
British life insurance

Reeling and dealing

Jul 8th 2004
From The Economist print edition

The slow tidying-up and consolidation of a tarnished industry



LATELY, British life insurance has seemed synonymous with disaster. Equitable Life, a mutual, nearly collapsed four years ago after promising policyholders more than it could pay. The mess is still being sorted out. Standard Life, another mutual, is also floundering. It wants to go public, after years of resisting, to boost capital; so far this year, it has taken in 11% less in life premiums than in 2003.

Indeed, the whole British market has been contracting (see chart). Regulators are trying to restore confidence in the British life industry, the world's third-largest. It boomed in the 1990s as Britons poured money into endowment policies, with which they hoped to repay their mortgages, and other life products. Then came the Equitable Life debacle and, as investment returns tumbled, a scandal about the mis-selling of endowments. Now regulators are trying to prevent companies skimping on capital. On July 2nd, the Financial Services Authority (FSA) published the final version of new rules, to take effect by the end of the year, that will oblige big life insurers to count their assets and projected payments to policyholders more carefully, and hold more capital accordingly. Amid the pressure to get sums right, many funds have closed to new business, as Equitable Life did in 2000.

There are good pickings amid the ruins. Swiss Re, the world's second-largest reinsurer, announced last week that it will pay £333m ($610m) to acquire Life Assurance Holding Corporation (LAHC), which administers over £5 billion in assets acquired from other insurers. Because LAHC's funds are closed to new business, Swiss Re can make good money from running the policies off, without the trouble of hunting for customers. The acquisition is the biggest yet of a British life company with closed books, according to Anthony Stevens of Mercer Oliver Wyman, a consultancy. Administering such closed funds is the speciality of Admin Re, the subsidiary of Swiss Re that made the purchase. It is strong in America and is building up its British holdings: last year it bought Zurich Life's closed British business for $240m.

More deals for closed funds look likely. Prices have come down, says Ned Cazalet, an industry consultant, because the FSA's new rules have forced insurers to understand their liabilities better. Old Mutual and Britannic, biggish insurers both, have been nosing around for closed businesses to buy. This week Abbey National, Britain's second-biggest mortgage lender, denied reports that part of its closed life business was on the market. The life business, all closed, of Royal & SunAlliance, another well-known name, is up for sale.

There is a catch. Whereas LAHC keeps mostly unit-linked holdings, more than half of Britain's policies have a “with-profits” structure. These are supposed to smooth out fluctuations in investment returns and pay fairly steady annual bonuses. But the calculation of charges and bonuses has been downright opaque. Equitable Life was the classic case. Such is the concern that the FSA's new regulations so far apply, in the life industry, only to with-profits funds. Given the bad press for these policies and the extra capital buyers may now need to get FSA approval for a deal, says Mr Stevens, with-profits businesses may be trickier to sell.

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Chicago's exchanges in Asia

The soy road

Jul 8th 2004 | CHICAGO AND LONDON
From The Economist print edition

The CME and CBOT set their sights on China and its neighbours

THE heads of America's two biggest futures exchanges are not shy about blasting their European rivals. But ask them about business prospects in Asia, and they talk in softer tones: they are “missionaries”, says one; doing “outreach”, says the other. The region is, believes Craig Donohue of the Chicago Mercantile Exchange (CME), the “next frontier”. These days he and his counterpart at the Chicago Board of Trade (CBOT), Bernard Dan, are often in Asia, especially China. Chinese officials are also frequent visitors to Chicago.

Asia's derivatives exchanges are mostly small. For instance, trading on the Tokyo International Financial Futures Exchange (TIFFE), a putative partner of the CBOT, hovers near 200,000 contracts a day, less than a tenth of the Chicago exchange's volume. Besides Japan, the main markets are in Singapore, South Korea and Taiwan. China made an abortive attempt at bond-futures trading a decade ago. It failed amid charges of price rigging and poor oversight. For the Chicago missionaries, the first task is education. Messrs Dan and Donohue are trying to convince government officials, regulators and even soybean crushers that derivatives, contrary to their reputation as dangerous and complicated, help companies manage risk and reduce price volatility.

Their efforts are hardly altruistic. The CME and the CBOT have grown fast in America, where together they account for 85% of futures trading. Despite competing for risk-management business in general, there is little overlap between their products, which range from commodity to currency and Treasury contracts. Each is making inroads into Europe, thanks to the rise of telecommunications hubs and proprietary trading shops in places like Gibraltar and Dublin. New hubs in Europe have boosted the CME's trading there to about 46,000 contracts a day, up from virtually nothing early this year. The CBOT is also considering a possible hub in Dubai.

And so to Asia, which Mr Donohue thinks could be a bigger market than America in 20 years' time. Already, he notes, South Korea's KOSPI 200 stockmarket-index future is the world's most actively traded, with around 1.6 billion contracts a year (although the value of these is small).

For now, at least, Asia has room for both Chicago exchanges. The CBOT—where more than 70% of the world's grain derivatives are traded—has set its sights on China, a huge importer of soybeans (for cattle feed) from the Americas. It plans to list and launch its own South American soybean contract, and is also working closely with China's Dalian Commodities Exchange. In newly liberalised Taiwan, Mr Dan wants to see retail investors trading American index products—and (why not?) Americans dealing in Taiwanese derivatives. Japan, which holds masses of American debt, is another priority, especially because TIFFE conveniently uses the same electronic-trading platform as the CBOT.

CME, which has been cultivating Asian ties for years, is marking different territory. In China it hopes to broaden access to the restrictive foreign-exchange market; Mr Donohue notes that setting up hedging and risk-transfer tools would help China move towards a free-floating currency. CME also aims to help the Shanghai Futures Exchange (which now mostly deals in copper, rubber and aluminium) launch China's first financial derivative. The CME would like to offer the popular South Korean KOSPI index contracts on its Globex electronic-trading platform, for use after Asian business hours. The exchange is also eyeing India, which has already shown an appetite for derivatives, and thinks near-term business will grow well in Australia and Singapore.

What has spurred these sudden ventures abroad, aside from Asia's rapid growth and opening markets? Battles back home, mostly. The CBOT has had to fend off Eurex, a German-Swiss rival and the world's largest futures exchange, which is trying to snatch a share of its Treasury business. Despite offering low

prices, Eurex has so far captured the merest sliver of the market. The CME, meanwhile, is facing a potential challenge from Liffe, another European exchange. Both European challengers have used electronic trading, and their forays seem to have spurred both Chicago exchanges not only to step up their technology investments, but also to get more aggressive abroad.

So who will gain most as the Chicago rivals head for Asia? Local players, for one. The strongest of these are starting to form partnerships with the big foreigners, who bring new business and in turn benefit from locals' distribution networks. Between the Chicago duo, Mr Donohue claims the edge for CME, because it is bigger and unlike CBOT it owns its electronic-trading platform and clearing house (the CBOT recently started using the CME's clearing facilities). Eurex, preoccupied with its American foray, has so far been less aggressive in the region, though it has ties to Hong Kong, Australia and Japan.

Much may depend on what happens at home. Both exchanges have just posted record volume in the latest quarter, but the CBOT may be having the better run. It has just reported the highest price ever paid for a trading seat and could vote on going public by the year's end. Meanwhile, the CME has had to weather the departure of three top officials: its chief executive and chief investment officer, who helped build Globex, and another executive, who now heads Eurex's American arm. For the new team, Asia beckons.

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Economics focus

A gentler touch

Jul 8th 2004
From The Economist print edition

The OECD softens its line on labour-market reform

ECONOMISTS have a well-deserved reputation as killjoys. They have long enjoyed pointing out the unintended consequences of government policies. Think of almost any programme, and an economist will pop up with a list of ways in which it will come back to haunt its political sponsors.

Take labour markets, which are especially rich in rules and regulations that are intended to help people but can often hurt them. Generous unemployment benefits, for instance, may provide a welcome safety net for people who lose their jobs, but they have costs too, not only in the taxes needed to finance them but also in perverse incentives for the unemployed to avoid work. Laws requiring big severance payments for sacked workers help people hang on to jobs, but also make firms less likely to hire in the first place. High minimum wages make some workers better off, but at the cost of reducing the overall supply of jobs and leaving some would-be workers out in the cold.

Until recently, the OECD, a club of mostly rich-country governments, could be relied on to make exactly such points and plead for reform, even though many of its members have often been slow to take its advice. Since it crafted its “Jobs Strategy” ten years ago, its reports on members' economies and its annual *Employment Outlook* have followed a consistent line: cut unemployment benefits; restrict the eligibility for disability insurance; reduce or remove minimum wages and restrictions on hours worked, such as France's 35-hour week; and trim generous severance benefits. While this often earned the OECD the ire of its member governments, the organisation felt free to deliver uncomfortable economic messages.

However, the *Employment Outlook* published on July 7th shies away from the fire-and-brimstone approach. This year and next the *Outlook* is dedicated to reassessing the OECD's previous line. This year's says that employment policies should take account of other “social objectives”, such as “a better reconciliation of work and family life” and “equity outcomes in line with national preferences”. This sounds much less hard-headed.

Although unemployment has fallen over the past decade in many countries, it is scarcely a thing of the past, especially in continental Europe. Despite an improving global economy, the OECD still forecasts an unemployment rate of 7% across its members in the coming year. And this figure only counts those who are actively seeking work. Many European countries have a disappointingly high proportion of working-age adults who are not in the labour force at all.

Troublingly, however, too few countries have made the wide-ranging reforms advocated by the OECD. Often, the laggards have been those that need them most, such as France and Germany. In several countries, the most that governments have done is to loosen protection for temporary workers, while leaving restrictions on firing permanent staff virtually untouched. But that has merely (and predictably, economists would say) caused employers to shift from permanent to short-term contracts, exacerbating inequality of treatment in the labour market. Arguably, partial reform has been worse than none.

Reform and reassessment

Nonetheless, according to the OECD's figures there remains a clear and strong correlation between high levels of employment protection and high levels of unemployment and inactivity. Job protection probably restricts the flow of workers out of jobs and into unemployment, as it is intended to do; however, it also reduces the flow out of the dole queue and into work.

All this should bolster the case for further reform. As the *Employment Outlook* shows, in the past few years the pace has slowed in some respects (and, in a few cases, gone into reverse). That said, reform need not mean stripping away all employment protection. Some countries are trying out inventive policies intended to allow companies to hire and fire more freely, yet still provide workers with some security of income if they lose their jobs and give them an incentive to look for work. The Netherlands, Denmark and New Zealand have employment rates close to America's, yet also manage to maintain big safety nets. The OECD's exploration of these examples is a saving grace for a document that is otherwise laden with platitudes about reconciling “social objectives”.

Take Denmark. It pays the unemployed up to 96% of the salary they received in work. You might think that this would not inspire them to seek a new job. Yet the Danish approach makes use of “activation” policies, such as monitoring the diligence with which the jobless seek work and offering full-time programmes for training. The disadvantage is that such an approach is expensive: it costs a huge 5% of Denmark's GDP.

The Austrian government has tried to address the problem of high severance costs, which can act as a disincentive to hire new workers. Employers now pay about 1.5% of employees' salaries into special individual accounts. Sacked workers with more than three years' tenure can either take the money or have it paid into a pension fund. This eliminates the high cost of firing workers without reducing the payout to sacked employees. There is a cost—in effect, a levy on wages—but the net effect seems to be that flows into and out of work are smoother.

The Netherlands has privatised its job-search agency, and pays a bonus for placing workers in jobs. It has also ensured that the unemployed would earn more working than from benefits. Its bigger neighbours would be wise to emulate this.

Such steps are welcome. Ministers are not due to discuss the OECD's review until 2006. The approach hitherto has been basically sound, even if some OECD economists are not so sure. More reform is needed. It would be a pity if politicians were given an excuse to stop now.

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Lie detection

Making windows in men's souls

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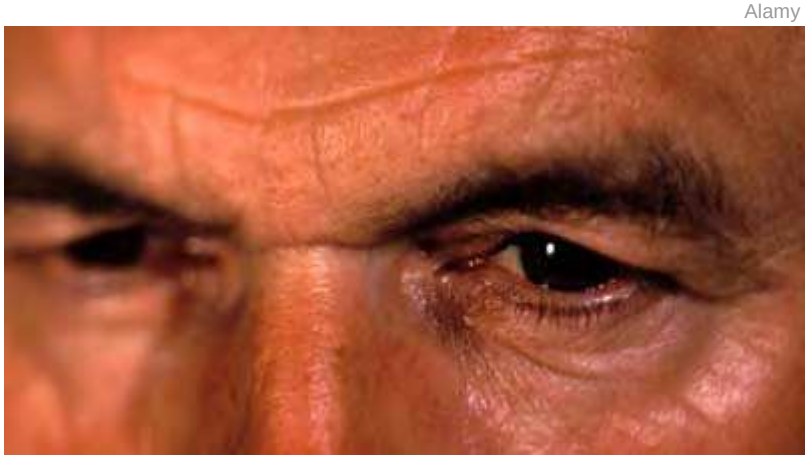
From The Economist print edition

Alamy



The science of lie detection has a chequered past. But it is becoming more reliable

THE truth, the whole truth, and nothing but the truth is a fine aspiration. But, as Pontius Pilate said to Jesus, “What is truth?” For decades, researchers have grappled with the problem of creating a machine that can tell, definitively, whether a person is lying. Until recently, their efforts have been unsatisfactory. The current generation of lie-detection technologies has been put under scientific scrutiny and found wanting. But science, ever resourceful, is coming up with new ideas. Soon, at least in some cases, that old courtroom platitude may itself come to resemble the truth more closely.

Mention the term “lie detector” to most people and they will probably think of the polygraph. This was invented in 1921. It looks at changes in a range of physiological phenomena—such as a person's breathing rate, pulse, blood pressure and perspiration—that take place while a suspect is being questioned. These are supposed to indicate if the answer given is untrue.

Polygraph evidence is accepted in many jurisdictions, notably in America. Although American military courts will not allow it, the only civilian courts there that have deemed it completely inadmissible are those of the District of Columbia and the Fourth Circuit (the group of states immediately south of the Mason-Dixon line). In other states its use is at the judge's discretion. Unfortunately for people in areas where they are still used, polygraphs do not work—or, more charitably, are easily duped. That was the conclusion of a report released in 2002 by America's National Academy of Sciences.

Another apparently promising candidate, voice analysis, does not seem to work either. There are repeated claims that tremors in a person's voice can reveal when he is lying. But a study by Mitchell Sommers of the University of Washington in St Louis, showed that—at least in the case of a system called Vericator—it is not as reliable as had been thought. Voice analysis can, Dr Sommers concluded, indicate an individual's level of stress. But that does not correlate with dishonesty.

The problem with both polygraphy and voice analysis is that they rely on second-hand signs of lying which a good actor can suppress. Furthermore, someone who is telling the truth might exhibit just these signals, because the very act of being questioned by the authorities is stressful. Instead, current research is looking directly at the source of lies, the brain itself.

Lies, all lies

Daniel Langleben, of the University of Pennsylvania, in Philadelphia, uses a brain-scanning technique called functional magnetic-resonance imaging to probe his subjects' honesty. The lie which those subjects are asked to tell is a small one: they have to persuade Dr Langleben, or one of his assistants, that they are holding a particular playing card when often they are actually holding a different one. Each successful deception earns a subject $20. The researchers have not had to hand out much cash, though. The brains of lying subjects light up in particular places—notably the anterior cingulate gyrus and left prefrontal cortex—in ways that they do not in the honest.

A second technique for probing the brain directly during questioning is the “cognosensor” developed by Britton Chance, who also works at the University of Pennsylvania. His subjects wear a headband that beams infra-red light through their skulls and into their brains. Part of this light is reflected back, and the pattern of reflection indicates activity in the tissue it has been reflected from—in particular, changes in the flow of blood to that tissue.

According to Dr Chance, different emotional disturbances have characteristic reflection patterns. And when a person lies, more of the light is reflected, and the reflections come from a wider area, than when he is telling the truth.

A third brain-probing lie-detection technique, based on electroencephalography (EEG), has actually made it out of the laboratory and into the courtroom. Lawrence Farwell, the founder of Brain Fingerprinting Labs in Seattle, Washington, calls it MERMER (memory and encoding related multifaceted electroencephalographic response). It is, he claims, 99.9% accurate at determining the veracity of certain sorts of statement.

MERMER works by hooking someone up to a standard EEG machine and asking him about specific details of, for example, a crime scene. Lack of a brainwave called P300 denotes lack of familiarity with the details in question, suggesting any denial should be taken at face value.

The technique has already stood up to legal scrutiny twice—once when it supported a conviction, and once when it freed an innocent suspect. It will soon be used again, in the appeal by Jimmy Ray Slaughter, from Oklahoma, against his conviction for murdering his ex-girlfriend, Melody Wuertz, and their 11-month-old daughter, Jessica, in 1991. MERMER suggests that Mr Slaughter had no recollection of important facts about the murder, such as which rooms the victims' bodies were located in.

Although not yet foolproof, these three methods do offer possible alternatives to the antiquated techniques of the polygraph. The truth is out there. It is just a question of finding it.

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Agricultural biotechnology (I)

Designer meat

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From The Economist print edition

Better breeding through biotech

Get article background

IN MANY countries, biotechnology and food are uneasy bedfellows. The wholesale rejection of genetically modified crops by consumers in much of Europe might have been expected to cause caution among firms interested in turning an honest buck from agricultural biotech. But as proponents of genetic modification are wont to point out, GM is as old as agriculture itself—for what is selective breeding for better plants and animals if it is not a form of genetic modification?

One way to get around consumer suspicions while taking advantage of modern genetic technology might be to do the actual genetic modification the old-fashioned way, by mating selected sires with selected dams, but to use biotech to decide which sires and dams to mate together. And that, indeed, is the business planned by MetaMorphix, a firm based in Savage, Maryland.

Two years ago, MetaMorphix acquired the livestock genotyping business of Celera, a company founded in 1998 to sequence the human genome. It then joined up with Cargill, a big agribusiness firm, to commercialise a genetic test that will help to reveal, prior to slaughter, a cow's propensity to produce desirable meat. That task is being accomplished by analysing thousands of so-called single nucleotide polymorphisms (SNPs) in the bovine genome. A SNP is a place where the genomes of individual animals vary by a single genetic “letter” (ie, one of the chemical base pairs that encode the information in DNA). SNPs are convenient markers for different versions of particular genes, and different versions of genes result in differences between animals. What MetaMorphix and Cargill are trying to do is find out which SNPs are associated with variations in meat quality—such traits as flesh colour, amount of marbling, wetness and tenderness—so that these can be identified before an animal is killed, and suitable animals thus be reserved for breeding.

Over the past two years, Cargill has studied 4,000 cattle, trying to correlate MetaMorphix's genetic markers with meat quality—and with other important traits, such as growth rate. Almost 100 useful SNPs have been identified from this study. The result is a prototype testing kit which the firm plans to start using in August. The first “designer meat” produced this way is expected to come to the supermarket shelves within a year.

Besides enhancing flavour, marker-assisted breeding may help to improve animal health and productivity. Pyxis Genomics, based in Chicago, has linked up with BoviBank, a Norwegian company, to identify SNPs that could enhance cattle's resistance to mastitis, an infection of the mammary glands. Meanwhile, several publicly funded programmes are under way with the goals of eradicating scrapie (a sheep disease similar to bovine spongiform encephalopathy, better known as mad-cow disease), and of producing cattle that are resistant to Johnes disease, a fatal bacterial infection of the small intestine.

The logical next step, having once bred a cow or sheep that has been optimised for a desired characteristic, would be to reproduce the result by cloning it. But cloning mammals has proved difficult, and even if it could be done routinely, it might not go down well with the average shopper. Using SNPs to keep animals breeding true, however, could not possibly offend anybody. Could it?

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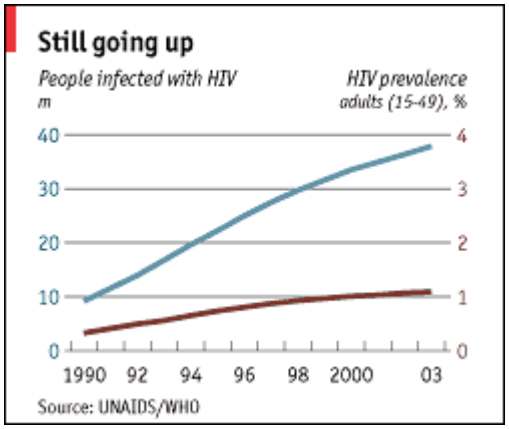
AIDS

Cold comfort

Jul 8th 2004
From The Economist print edition

More miserable data on AIDS

Get article background



IT IS good news of a sort: the officially recorded number of people infected with HIV, the virus that causes AIDS, is slightly less than was previously thought. A figure the wrong side of 40m has now been revised to 38m, owing to the employment of better methods for collecting statistics. The unequivocally bad news, though, is that the figure is still rising. That is the message of the "2004 Report on the Global AIDS Epidemic", which was released on July 6th by UNAIDS, the United Nations agency assigned the task of combating HIV.

The report is issued every two years, in the run-up to the biennial International AIDS Conference, the 15th of which will start in Bangkok on July 11th (and will be reported on in next week's issue of *The Economist*). This year's report emphasises the rising proportion of women who are victims of the virus. In Africa, where the epidemic is oldest, 57% of those infected are female. In countries where HIV has arrived more recently, the preponderance of victims tends to be male. That is because the early spread of the virus tends to be associated with behaviours such as intravenous drug injection and promiscuous sex (both homosexual and heterosexual) that are more frequently indulged in by men than women. Once an epidemic has become established, however, the equation changes. The data suggest that for any given act of heterosexual intercourse in which only one participant is HIV-positive, a man is twice as likely to infect a woman as a woman is a man.

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Agricultural biotechnology (II)

Tough tomatoes

Jul 8th 2004
From The Economist print edition

Genetic technology supports sustainable farming

Get article background

NEW genetic technology may not only help to bolster traditional selective-breeding techniques (see article). It may also, horror of horrors, have a role in the sort of “sustainable” farming favoured by opponents of high-tech agriculture. For biotech has now shown that there are differences between the molecular biology of sustainably grown crops and those grown using modern agricultural techniques. Moreover, those differences favour the sustainably grown plants.

Autar Mattoo and his colleagues at the American Department of Agriculture's Vegetable Laboratory have been comparing mulching methods for tomato crops. As they observe in the *Proceedings of the National Academy of Sciences*, they have identified differences in the ways that tomato plants express their genes, depending on whether those plants are grown on a black polyethylene mulch and fed with synthetic fertiliser (the method favoured by conventional modern horticulture) or by using a mulch made from a leguminous plant called hairy vetch (which is favoured by the proponents of sustainability).

Black polyethylene mulching involves the plants growing through holes in plastic sheets that cover the soil. The sheets keep the soil moist and warm, and also stop weeds growing. Hairy-vetch mulch does all of those things, too, but using it is not as convenient as laying down a few sheets of plastic, and is more expensive. On the other hand, plants grown using hairy-vetch mulch are a lot healthier (and yields are 20% higher), so Dr Mattoo wondered if he could track down the biochemical origins of this healthiness.

To look at the activity of the plants' genes, Dr Mattoo used a modern genetic technique called cDNA subtraction cloning. This works by making copies of the messenger molecules that carry information from the genes in a cell's nucleus to the protein factories in its outer reaches. The more messengers there are from a particular gene, the more active that gene is. The copies of the molecular messengers are known as complementary (or “c”) DNAs, and by employing suitable chemical trickery, it is possible to compare the cDNA profiles of two plant tissues by, in effect, subtracting one from the other, so that only the differences remain.

Using this technique, Dr Mattoo found a number of genes that expressed themselves more vigorously in plants grown on hairy-vetch mulch, rather than black plastic. These genes included those involved in photosynthesis, disease resistance, defence against pests and the assimilation of nitrogen. All of this helps to explain the more vigorous growth of hairy-vetch-mulched plants.

What is not explained, however, is why these genes express themselves vigorously. But Dr Mattoo has a hypothesis. Among the healthiest parts of the hairy-vetch-grown plants are their roots. These are a source of hormones which affect gene expression. More roots, more hormones, and more expressive genes. One up to sustainability.

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Veterinary technology

On the hoof

Jul 8th 2004
From The Economist print edition

New designs are being trotted out for horseshoes. Square toes are in

AP

Horseshoes are sooo last year, dahling

IF TIRED and aching feet are ever a problem for you, imagine how bad things could get with four feet to look after instead of just two. Researchers in the Structure and Motion Laboratory at the Royal Veterinary College (RVC) in London spend a lot of time thinking about such matters, and at an exhibition held at the Royal Society in London on July 6th, some of them explained the latest developments in equine footwear.

A traditional horseshoe is a hard loop of steel that is nailed to the animal's hoof to prevent the horny keratin of which that hoof is made from chipping, cracking or splaying. It is an effective solution, but one that goes back millennia. The RVC is one of many groups that are trying to bring the humble horseshoe into the 21st century.

One approach discussed at the exhibition draws on the work of Gene Ovnicek, an American farrier. His work on wild horses showed that their feet tended to wear in four places. That finding led to the development of a square style of horseshoe that has come to be called the Natural Balance Shoe.

This was originally designed as a remedial shoe for horses with problem feet, according to Nicola Smith, a research student in biomechanics at the RVC. Such problems might include collapsed heels and weak hoof-horn. The Natural Balance Shoe, though, is causing controversy. In some cases it is starting to replace traditional shoes for normal use. Yet work by the RVC shows that it is not a better shape of shoe for the average horse.

The Natural Balance Shoe, in any case, is still made of metal, and one might be forgiven for wondering why horse owners do not just pop their equine pals into a nice, comfy set of running shoes instead of all this business with nails.

Part of the reason, according to Miss Smith, is that on many surfaces rubber-soled shoes would be no use. When a horse is galloping, its hooves hit the ground at about 15kph, and this causes damaging vibrations in the animal's legs. One way of reducing these vibrations is to allow the hooves to skid a bit when they hit the ground. Rubber-soled shoes will skid on grass, but on most other surfaces they tend to develop too much friction.

That does not mean, however, that you have to stick with traditional (or even Natural Balance) horse shoes. Shoes made of hard plastic may improve matters, especially as they can be glued rather than nailed on to hooves. So, for horses that spend a lot of time walking on artificial surfaces such as tarmac, the RVC is currently experimenting with plastic shoes that have tungsten carbide surfaces to provide the right amount of friction.

One of the most innovative versions of a plastic shoe is the Imprint Therapeutic Shoe, made by Andrew Poynton, a high-tech farrier who works in Malmesbury, England. Mr Poynton's shoe is made of mouldable plastic. To fit it to a horse you warm it up to soften it, and mould it around the animal's hoof. Then you set it solid by chilling it with an aerosol. Like all high fashion, such shoes are expensive. In Britain, traditional shoeing costs about £70 ($130) an animal. Fitting your nag with Imprint Therapeutics on all

feet could set you back £400. But for the fashionistas of the equine world, it may be worth it.

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About sponsorship

China's environment

No economic fire without smoke?

Jul 8th 2004 | HONG KONG
From The Economist print edition

ROPI

Exaggeration of China's environmental problems does not help to resolve them

AS CHINA explodes economically, it is imploding ecologically. The flipside of the country's rapid growth is a worrying degradation of its environment. According to the World Bank, it is home to 16 of the 20 most polluted cities in the world, while deforestation (begun centuries ago) has turned a quarter of the country into desert. With only a tenth as many cars, Beijing pumps out as much carbon monoxide as Los Angeles and Tokyo combined.

As described by Elizabeth Economy, a director of Asia Studies at the Council on Foreign Relations, an American think-tank, the scale of China's environmental degradation is shocking. Her book is particularly strong in its examination of the peculiarly Chinese reasons—beyond the country's rapid development and huge population pressure—that lie behind this: the leadership's obsession with short-term growth to preserve social stability, whatever the ultimate cost, is one; the weak rule of law and a tradition of devolving power to the regions, where watchdogs and polluters are often in collusion, is another. On paper, there is a ministry and a set of laws designed to protect the environment. In practice, China's environmental agency, SEPA, has a staff of 300, a small fraction of its American equivalent. Moreover, it has little standing in Beijing and practically no resources.

There is, of course, a good reason why America pays more attention to its environment than China does: it can afford to. Until more people get richer, China may not have the resources or the willpower to care much about pollution. Ms Economy more or less ignores this trade-off and concentrates on the negative consequences of economic growth. And at times she uses questionable statistics to support her argument—for example, her assertion that children living in Chinese cities are doing the equivalent of smoking two packets of cigarettes a day is lifted from a local newspaper and is hard to verify.

Ms Economy holds out the hope that local non-governmental organisations (NGOs) will compensate for China's institutional shortcomings. By one count there are now 2m of these, and the book includes profiles of several courageous

The River Runs Black: The Environmental Challenge to China's Future
By Elizabeth C. Economy

Cornell University Press; 337 pages; $29.95 and £17.50

Buy it at
Amazon.com
Amazon.co.uk

The Retreat of the Elephants: An Environmental History of China
By Mark Elvin

individuals who are trying to change things. But the vast majority of them are no more than individuals fighting single issues with little funding. The Communist Party immediately outlaws anything more ambitious that could threaten its authority.

The book pays insufficient attention to another influence for change: the positive impact of foreign multinationals. While these may not operate with quite the same clean technology as they do at home, their standards are still far higher than those of their local rivals.

Yale University Press; 564 pages; $39.95 and £25

Buy it at
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Amazon.co.uk

The New Consumers: The Influence of Affluence on the Environment
By Norman Myers and Jennifer Kent

Island Press; 192 pages; $24 and £18.50

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Chopped and changed

China has been at war with its environment for centuries. Mao's declaration that man must “conquer and change nature and thus attain freedom from nature” echoed traditional Confucian beliefs of social order, in which the earth's role was to provide for humanity. Mark Elvin, an environmental historian and China scholar, chronicles how early emperors chopped down forests, diverted rivers and laid waste to fields as part of their constant warfare. As a result, in 4,000 years the elephants of his title retreated from all over China into a tiny corner of the south-west.

Mr Elvin's book is massive in scope and peppered with classic texts and ancient Chinese poetry. But the end result is disappointing. Its rambling sentences and mathematical equations leave the reader more irritated than fascinated.

While Mr Elvin details the past, Norman Myers, an Oxford University academic, looks to the future. His book, which is as lightweight as Mr Elvin's is ponderous, describes the imminent rise of 1.1 billion “middle-class consumers” in the developing world—40% of them from China and India alone—and the pressure they will put on the world's ecology. Mr Myers reels out statistics to prove that buying cars and washing machines will ruin developing countries' environments. But once again he ignores the changed attitudes to pollution that come with greater wealth.

China is using its natural resources to lift the living standards of its people as rapidly as possible—as the developed world did (and still does). Its main problem is the huge short-term cost of this: the World Bank estimates an annual 8-12% of China's GDP now goes on medical bills, lost work and disaster relief. This sum is growing and could eventually threaten economic growth itself. Another concern is political: in democratic countries, affluence leads to demands for a cleaner environment. In China, there is no mechanism for people's wishes to influence government policy directly, unless (and until) the Communist Party loses its grip on power.

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Michael Moore

Sinned against

Jul 8th 2004
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An attack on the maker of Fahrenheit 9/11

MICHAEL MOORE is a controversial phenomenon who has made a name for himself by opposing big business and the political establishment in America. His new film, “Fahrenheit 9/11”, has recently broken box-office records for a documentary. But Mr Moore's reach sometimes exceeds his grasp, and he often seems to be a disagreeable employer and colleague. Many on the left, who might have been expected to constitute his natural base of support, have written persuasive critiques of his work.

Criticism from the right, of which this book is one example, has been generally less astute. “Michael Moore is a Big Fat Stupid White Man” is edited (and the bulk of it is written) by a pair of Moore-obsessed bloggers. David Hardy set up a website called mooreexposed.com, while Jason Clarke founded moorelies.com. The book is the sort of crackpot melange that can work online—as in the drudgereport.com—but set in dignified print it too often looks just plain daft. At one point, for example, the authors liken Mr Moore to Hitler, and at another to Sayyid Qutb, an ideological theoretician of the Muslim Brotherhood, an extremist group founded in Egypt in the 1920s.

Michael Moore is a Big Fat Stupid White Man
By David T. Hardy and Jason Clarke

Regan Books; 240 pages; $22.95 and £12.99

Buy it at
Amazon.com
Amazon.co.uk

Of the 18 repetitive essays that make up the book, five were written by outside contributors, seemingly chosen at random. Of these, one is a review of “Bowling for Columbine”, a previous Moore film, taken from an Australian newspaper. It ends on the intellectual high note, “Go to hell, Mikey!” This level of argument is hardly the sort of thing to sway anyone who does not already share the authors' maniacal dislike of Mr Moore. Indeed, their loathing leads them not only to *ad hominem* attacks but also to exaggerate Mr Moore's influence. After all, his audience is no bigger than those of his demagogic counterparts on the right, such as Rush Limbaugh.

Only one of the essays, “America's Left Surrenders Itself to the Giant Sulk” by Andrew Sullivan, a former editor-in-chief of *New Republic* magazine, rises to a level of cogency sufficient to raise legitimate questions about Mr Moore's methodology and style. The short essay, taken from the *Times*, is a bit of journalistic ephemera, but at least it does not resort to fatuous popular psychology, as the book's authors do, although it does make the cheap charge that Mr Moore is “anti-American”.

It is possible to take issue with Mr Moore's work without chauvinistic jibes and xenophobic rhetoric. This book unwittingly apes the filmmaker's over-the-top style. Its heavy-handed and self-congratulatory manner utterly defeats its purpose.

Michael Moore is a Big Fat Stupid White Man.
By David T. Hardy and Jason Clarke.
Regan Books; 240 pages; $22.95 and £12.99

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About sponsorship

Women travellers

Running away from home

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SOMETIMES they played the part, like Lady Hester Stanhope (1776-1839) with her Turkish pipe and turban, or Amy Johnson (1903-41), posed in pilot's goggles and leather headgear. But more often—at least in the 19th century, when women took to the deserts and forests in some numbers—the travellers who feature in an exhibition which opened on July 7th at London's National Portrait Gallery dressed themselves like maiden aunts, in perfect imitation of the conventions they defied. There is stern-looking Constance Gordon Cumming (1837-1924), ruched, trimmed and upholstered in Victorian silk; and there is Isabella Bird (1831-1904) with her umbrella, face grimly tied up in hat ribbons, looking like the old Queen Victoria.

Off the Beaten Track: Three Centuries of Women Travellers
By Dea Birkett

National Portrait Gallery Publications; 144 pages; £18.99

Buy it at Amazon.co.uk

Nothing could have been more deceptive. The lives of these women were not at all like those of their Victorian sisters. The dour Constance, for example, describes herself naked in a Fijian stream, hair undone and eating oranges plucked straight from the trees. Mary Kingsley (1862-1900)—another pursed face in hat strings—fell into West African swamps, and exchanged fetishes and fish for hairpins and alcohol. Most of them ostentatiously shunned feminist causes. For women like these, it was home life that was the real hardship.

Home meant confinement—“walls and gardens”, as Gertrude Bell put it. It meant years of looking after ageing parents and feckless brothers while “fighting a burning desire in my own heart”, as one of them wrote, “that craved for the whole world”. Home made Isabella Bird physically ill. Abroad, she could spend eight hours in the saddle and sleep soundly out of doors. But in England she suffered insomnia, depression and mysterious spinal complaints. “I find the society of English people fatiguing”, she once wrote after some months in the Far East. “My soul hankers for solitude and Freedom.”

Dea Birkett's lively and informative book, published to coincide with the exhibition, resounds with this word, often written thus, with a capital letter. The author dashes through the centuries, from the early fourth to the late 20th, dividing her subject into categories: adventurers; companions; scholars; and writers and artists. Among these there is some overlap, for the scholars were also writers, and the companions were sometimes adventurers, and so on. But with all of them, there is a palpable sense of exhilaration.

Women travelled primarily for the joy of it. They had no theoretical axes to grind. As botany, geology, anthropology and other once amateur pursuits were gradually fenced off into all-male professions, so women struggled for education, funds and recognition. It was frustrating. But it meant that they were forced to travel simply, with little parade, either conceptual or actual. (Henry Morton Stanley, we learn, took eight tonnes of equipment on his first African expedition, carried by 300 porters.)

The charge against women—that they were good only for facts and particulars—turned out to be their strength. More dependent upon local help, they came closer to the worlds they were observing. Less learned, they were more open to impressions, more susceptible to the unexpected. In the foreword to the book, Jan Morris, a travel writer who was James Morris before she changed her sex, concludes that the vulnerability of women, and everything that goes with that, has made travelling easier for them than for men. And she, after all, should know.

Off the Beaten Track: Three Centuries of Women Travellers.
By Dea Birkett.
National Portrait Gallery Publications; 144 pages; £18.99

“Off the Beaten Track: Three Centuries of Women Travellers” is showing at the National Portrait Gallery, London, until October 31st

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Women in chess

Queening it

Jul 8th 2004
From The Economist print edition

THE queen is the most powerful piece on the chess board, and the only female. That may seem odd for a war game that probably originated in India around 500AD and quickly spread to Persia and Arab lands, not the sort of places where women held powerful jobs. But the queen, it turns out, was a latecomer to the game. In its first few centuries, the king's helpmate was a male vizier, or adviser, a feeble character who kept his head down while elephants (early bishops), horses (early knights) and the rest fought it out. It was not until around 1000AD that the vizier turned into a queen, and it took a further 500 years for the queen to acquire the deadly mobility she has today. Modern Muslim chessboards still stick to viziers.

Marilyn Yalom, an American academic whose previous books include such intriguing titles as “The History of the Wife” and “The History of the Breast”, links the rise in queenly power on the chessboard with the increase in power held by real-life queens. On a quick gallop round Europe's courts over eight centuries, she does indeed turn up a galaxy of formidable female rulers, from Eleanor of Aquitaine to Russia's Catherine the Great (though Britain's Queen Victoria gets no mention).

Birth of the Chess Queen: A History
By Marilyn Yalom

HarperCollins, 304 pages, $24.95. Pandora Press; £19.99

Buy it at
Amazon.com
Amazon.co.uk

In the high Middle Ages, chess became a popular pastime for the upper crust, both men and women. “The Book of Chess” by a 13th-century Dominican friar, Jacobus de Cessolis, was translated from Latin into a number of European languages and became a late medieval bestseller. By then, the game had changed character and become an allegory of society and, increasingly, a metaphor of love. Famous practitioners, such as Tristan and Iseult or Lancelot and Guinevere, were portrayed playing chess. “The Edifying Book of Erotic Chess”, published around 1400, was, in effect, a manual of seduction.

Come the Renaissance, come the inevitable backlash, both on and off the board. In 1534 a French poet, Gratien du Pont, published a chessboard with 64 rhyming insults to females, one for each square. Women still sat on thrones, and some of them, such as Catherine de Medici, still played chess. But by the 17th century the female *crème de la crème* had lost interest in the game. A survey in 2000 showed that women accounted for only 5% of the world's chess players.

So what are we to make of Ms Yalom's claim that the historic rise of the chess queen reflected the growing power of real queens? In the sense that the chess queen must have been modelled on real-life examples, fair enough; where there were no female rulers, as in the Arab world, there was no place for a chess queen. But reading through these brief accounts of historic European queens, it is impossible not to be struck by the fact that every one of them got to the top through men—fathers, husbands, sons—and even then managed to hang on only through sheer determination. This was no golden age.

Now, of course, things are different. In these days of equal opportunities, if the chessboard truly mirrored life, half the bishops, rooks and pawns would be female. Instead, the game has remained unchanged for 500 years. But whether or not you buy its thesis, this is a well-researched and enjoyable book.

Birth of the Chess Queen: A History.
By Marilyn Yalom.
HarperCollins, 304 pages, $24.95. Pandora Press; £19.99

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About sponsorship

Marlon Brando

Beyond the waterfront

Jul 8th 2004
From The Economist print edition

Can an actor appear in so much rubbish and still be great?

EPA

"IF THERE is a better performance by a man in the history of film in America, I don't know what it is." That was Elia Kazan on Marlon Brando, whom he directed in the Broadway and Hollywood productions of "A Streetcar Named Desire". They were big claims. Could anyone hope to live up to them?

Younger moviegoers, whose memories of Brando focus primarily on his truly dreadful work in film after lousy film between the 1960s and his death on July 1st at the age of 80, could be forgiven for doubting. Could anything be more deplorable than the half-wit he played in "Bedtime Story"? And is there a more embarrassing spectacle than his gingham-clad "granny" routine in "The Missouri Breaks"? Sceptics point to these as the performances of a lazy actor coasting on a titanic reputation.

What, after all, did he achieve? He had a facility for accents: Japanese in "The Teahouse of the August Moon"; German in "The Young Lions"; and even an English public school accent in "Mutiny on the Bounty". But other actors, from Sir Alec Guinness to Peter Sellers, have been good mimics, and it is not on that alone that their fame rests.

Many say that "The Godfather" (1972), which gave Brando his best-remembered role—as a Sicilian-American gangster—came not a moment too soon. By 1969 he was already reduced to appearing in second-rate features, such as "The Night of the Following Day", or to seeking work abroad, as in "Queimada!". "The Godfather" earned Brando his second Oscar, but wasn't even that a bit hammy?

Maybe. But definitely not hammy were his first six screen roles, beginning with "The Men" in 1950 and culminating four years later with "On the Waterfront", for which he earned his first Oscar. Realism on screen had never seemed so real. Brando slurred his words, spoke through a mouthful of food, delivered lines as if newly minted from his own pygmy brain. Was he just playing himself? Many thought so.

Then he played Mark Antony in "Julius Caesar" (1953) and the cynics were silenced. The scene in which he enters the senate after Caesar's murder, acknowledging none of the conspirators but gliding regally past as if they did not exist, points vividly to the play's denouement. For this, credit Marlon Brando, not Shakespeare. Ask if Rod Steiger, James Dean or Paul Newman, who all, like Brando, graduated from the Method school of acting, could have matched his Mark Antony, and the answer is a definite no.

In "On the Waterfront", Brando's longshoreman disregards past loyalties to arrive at his own sense of what is right and wrong. The characterisation lifts the film to a heroic dimension that is only hinted at in Budd Schulberg's script. It is a mesmerising performance that elucidates a great film, the last of an extraordinary series on which, ultimately, Marlon Brando's enormous stature will rightly rest.

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About sponsorship

Filming overseas

Relocation, relocation, relocation

Jul 8th 2004
From The Economist print edition

Filmmakers think again about where to shoot

Alexander of Morocco, lured by cheap extras

EWAN MCGREGOR, the Scottish star of Hollywood fare such as "Big Fish", is due to arrive in New York this month after a three-month tour on a motorbike filming in some of the world's most dangerous countries. Mr McGregor is rumoured to have been insured for over $35m while travelling through places such as Kazakhstan and Mongolia with his actor friend Charley Boorman (son of director John).

The rising costs of security are taking ever bigger chunks out of film and television budgets. When the war in Iraq persuaded Brad Pitt's insurers that they could not provide the top-ranking star with cover while shooting "Troy" in Muslim Morocco, the producers switched the set to Mexico. The costs of such relocation can be enormous—for big budget movies, as much as $400,000 a day. Shifting Troy's main cast and crew of hundreds cost even more than expected. The filmmakers had to withstand a Mexican hurricane that caused more damage than most terrorists could have hoped for.

Despite last year's suicide bombings in Morocco and increasing evidence of Islamic fundamentalism, some big-budget western movies have continued to film in the country. Sir Ridley Scott, a British director, brought his crew and stars over from Spain earlier this year to film "Kingdom of Heaven", a politically sensitive film about Saracens and 12th-century Crusaders that is due for release in May next year. Security was tightened on the set recently when a rumour spread that the film was to feature a crusader stamping on the Koran.

Two movies based on the life of Alexander the Great also planned to use Moroccan locations. Although one of them, directed by Baz Luhrmann, shifted locations to his home country of Australia after the terrorist bombings, Oliver Stone continued to use Morocco as the backdrop for his story of the peripatetic Macedonian. Due out in November, it is the most expensive independent film ever shot outside America. Without the benefit of Morocco's main attraction—extras that can be hired for around $1.80 an hour, plus a sandwich lunch—it would have cost much more.

The security problem pre-dates September 11th. Iain Smith, one of the producers of Mr Stone's "Alexander", faced death threats and protesting mobs when filming "City of Joy" in Bengal in the early 1990s. Then, in 2000, when he was in Israel about to start filming "Spy Game", starring Robert Redford and Brad Pitt, the latest Palestinian *intifada* began. The film had to shift to a fall-back location, at a cost of $5m-6m, but still managed to keep within its budget. The ability to relocate depends largely on the stage of production that the film is at when the trouble strikes. Mr Smith says that "the riskiest time on a shoot is two-thirds of the way through."

A growing number of film producers use western consultants to advise them on security. Andreas Carleton-Smith, president of Control Risks Group (CRG), the consultants who advised Mr Smith, says that the entertainment industry has lagged behind mainstream business in recognising the dangers of working abroad. CRG offers an assessment of the risks at different proposed locations, provides bodyguards for the main stars and draws up plans for a rapid evacuation should the need arise.

The producers of "Alexander" had additional help from the Moroccan gendarmerie, which patrolled the set's 15-mile perimeter. Morocco is trying to entice more western filmmakers to its fabulous landscapes

of mountains, sea and sand, and it recently won the right to continue to subsidise its fledgling film industry in a trade deal with America.

Many producers maintain that the risks from terrorism are greatly exaggerated. They say that the paparazzi are far more likely to impede film shoots than members of al-Qaeda. Sir Ridley closed the set of “Kingdom of Heaven” to terrorists and journalists alike. Mr McGregor's producers were just as anxious about pot-holes in Ulan Bator and freaks of nature as they were about kidnapping or sabotage. In “Alexander”, the actor Colin Farrell sustained a fracture, not in smiting the Persians or fending off the local *fedayeen*, but by tripping over some stairs when heading for dinner.

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About sponsorship

Obituary

Dimitry Dudko

Jul 8th 2004
From The Economist print edition

Father Dimitry Dudko, Russian dissident and recanter, died on June 28th, aged 82

BETWEEN 1964 and 1970, Dimitry Dudko kept a diary of the people he baptised. He reckoned there were three or four adults a day, and “countless children”. They were mostly baptised in a room in his house, which was piled high with books and icons. It was safer that way. Father Dimitry had discovered that if babies were baptised in church, activist members of local party committees would copy the name from the register and inform the parents' employers.

Under communism, the Russian Orthodox Church was not banned; but it had agreed, ever since a pact with the Bolsheviks in 1927, that it would be utterly subservient to the state. Father Dimitry, despite his look of elfin benevolence, was not subservient. He believed he was fighting a war. “We are in the front lines,” he told his congregation on Easter Sunday, 1977:

> And this front line is everywhere. We are surrounded by atheists on all sides. There is no place where there is no shooting going on. The press, art, theatre, schools, institutions—everything has been occupied by the atheists. The laws are all directed towards our suffocation...but we are alive!

Unlike other dissident clergy, who favoured secrecy and conspiracy, Father Dimitry used a priest's sharpest weapons: teaching, preaching, writing, the sacraments. His books were published abroad and in *samizdat* ; his sermons were handed round. (The Easter sermon of 1977, which became famous, was signed “A soldier of the Russian army”.) Illegally, he encouraged young people to discuss their experiences of God. Western radio stations carried his broadcasts. As a result, Russians and foreigners alike flocked to him, and he became for a while the West's favourite dissident priest.

The Orthodox Church reveres its martyrs, and Father Dimitry seemed to relish the prospect. Not only he, but the whole of Russia, was suffering a Golgotha from which resurrection would come. He had already spent eight years in a labour camp, as a young seminarian, for writing religious poetry during the second world war. As a priest he was harried by the KGB, moved from parish to parish to frustrate his pastoral work, and eventually ended up in a village church along the Shchelkovsky highway. Once he was hit by an ambulance, seemingly on purpose, and taken to a “hospital” guarded by police. Loyal seminarians managed to steal him away.

When, in 1980, he was arrested for giving “slanderous materials” to a man from the *New York Times*, it seemed that the moment of martyrdom had come. But then the unthinkable happened. Father Dudko, after six months behind bars, appeared on television to read, nervously, from a typewritten paper. His struggle against godlessness, he admitted, had really been a campaign against the Soviet state, and he

was sorry for what he had done.

His followers could not believe it. Perhaps he had been drugged or tortured; possibly, since he had been allowed to speak so publicly, he himself had been a KGB agent all along. Perhaps the Moscow Patriarchate had put pressure on him. The clerical authorities, after all, had always found him an embarrassment.

Father Dimitry himself never satisfactorily explained his recantation, though it ended his mission as a dissident priest. It was not until the post-communist years that some light was shed on the subject. In the 1990s Father Dimitry began to keep company with nationalists and communists, writing messianic articles for an ultra-nationalist and anti-western newspaper called *Zavtra* (“Tomorrow”). His columns revealed a nostalgic fondness, not uncommon in newly liberated Russia, for the iron hand of authority. Less commonly, he wrote of his reverence for Stalin, “a man given to us by God”.

At first, his Stalinism seemed almost more shocking than his “tele-repentance”. His own father had been arrested in 1937 for refusing to join a collective farm. Yet for Father Dimitry, Stalin had also been the strong man Russia needed. When faced with a choice between the new, brassy, chaotically capitalist Russia, in love with western ideals of wealth and promiscuity, and the austere, autocratic communist model, Father Dimitry chose the latter as better for the Russian soul, and closer to it.

He had meant what he said on that awful day in 1980: it was atheism he hated, not the apparatus of the communist state. Firm rule was necessary, as long as it could be improved by Christian principles. Patriotism, too, was necessary, to keep Russia secure from the enemies both within and without that sapped her moral fibre. And priests, by and large, should obey.

Father Dimitry's dilemma had been that of the whole Russian Orthodox Church. Under communism, he vacillated between fighting with, and compromising with, a godless state. After 1991, he had to decide whether Russia's spiritual rebirth would be achieved more effectively by chauvinistic nationalism, or by democracy. In each case, it could be argued, he decided the wrong way. But as the Moscow Patriarchate and the Russian Church Abroad—the “red” and “white” hierarchies, divided for almost 80 years—begin at last to draw together, Father Dimitry's struggles should be on the conscience of every believer who wonders which path the reinvigorated church should take.

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Overview

Jul 8th 2004
From The Economist print edition

Employment growth in **America** has slowed after several months of strong gains. Only 112,000 new non-agricultural jobs were created in June, less than half as many as analysts expected. The unemployment rate was unchanged at 5.6%. Average hourly earnings rose by 2.0% in the year to June, a decline in real terms.

Unemployment in the **euro area** remained at 9.0% for the third consecutive month in May. **Luxembourg** and **Austria** have the lowest jobless rates, at 4.2%, whereas **Spain** has the highest, at 11.1%.

Germany's jobless rate remains stubbornly high, at 10.5% in June according to national statistics. Measured on a basis harmonised across the EU, Germany's unemployment rate is 9.8%.

Retail sales in the **euro area** fell by 1.3% in May, the biggest monthly fall in six months; over the year to May, they fell by 0.9%. Retail sales in **Germany** fell by 2.3% in the 12 months to May.

Industrial production in **Britain** rose by 1.3% in the 12 months to May, up from 0.9% in the year to April. Output in the manufacturing sector, which has had a miserable time over the past few years, grew by 2.0% in the 12 months to May.

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Output, demand and jobs

Jul 8th 2004
From The Economist print edition

% change on year ago

	GDP latest		GDP qtr*	The Economist poll GDP forecasts 2004	2005	Industrial production latest		Retail sales (volume) latest		Unemployment % rate latest		year ago
Australia	+ 3.2	Q1	+ 0.9	+ 3.5	+ 3.4	– 1.1	Q1	+ 7.7	Q1	5.6	Jun	6.1
Austria	+ 0.5	Q1	+ 0.8	+ 1.6	+ 2.1	+ 5.6	Apr	+ 2.6	Mar	4.2	Jun	4.4
Belgium	+ 2.0	Q1	+ 3.0	+ 2.2	+ 2.1	– 1.0	Apr	+ 0.9	Apr	12.4	Jun†	11.6
Britain	+ 2.7	Q4	+ 4.2	+ 3.2	+ 2.7	+ 1.3	May	+ 7.4	May	4.8	Apr††	5.1
Canada	+ 1.6	Q1	+ 2.4	+ 3.0	+ 3.4	+ 2.8	Apr	+ 4.9	Mar	7.2	May	7.9
Denmark	+ 1.4	Q1	+ 3.8	+ 1.9	+ 2.2	+ 1.7	May	+ 1.5	May	6.5	May	6.0
France	+ 1.7	Q1	+ 3.1	+ 2.2	+ 2.2	+ 1.1	Apr	– 1.1	May	9.8	May	9.7
Germany	+ 1.5	Q1	+ 1.8	+ 1.4	+ 1.7	+ 2.2	Apr	– 2.3	May	10.5	Jun§	10.6
Italy	+ 0.8	Q1	+ 1.8	+ 1.2	+ 1.8	+ 0.2	Apr	– 1.6	Apr	8.5	Jan	8.9
Japan	+ 5.6	Q1	+ 6.1	+ 4.4	+ 2.2	+ 4.2	May	– 0.5	Apr	4.6	May	5.4
Netherlands	+ 0.9	Q1	+ 2.8	+ 1.3	+ 1.8	– 0.8	May	– 1.7	Apr‡	6.5	May**	5.1
Spain	+ 2.8	Q1	+ 2.6	+ 2.8	+ 2.8	+ 2.9	May	+ 1.2	May	11.1	May	11.3
Sweden	+ 2.6	Q1	+ 2.6	+ 2.8	+ 2.5	+ 4.3	Apr	+ 5.4	May	5.3	May†	4.2
Switzerland	+ 1.5	Q1	+ 1.6	+ 1.9	+ 2.0	+ 4.5	Q1	+ 1.6	Apr	3.7	Jun†	3.6
United States	+ 4.8	Q1	+ 3.9	+ 4.6	+ 3.6	+ 6.3	May	+ 7.3	May	5.6	Jun	6.3
Euro area	+ 1.3	Q1	+ 2.3	+ 1.8	+ 2.0	+ 1.7	Apr	– 0.9	May	9.0	May	8.9
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	+ 2.7	Q1	+ 3.0	na	na	+ 7.2	May	+ 5.7	Apr	11.6	May†	11.4
Greece	+ 4.0	Q1	+ 3.0	na	na	+ 1.8	Apr	+ 5.6	Apr	na		na
Iceland	+ 4.9	Q1	na	na	na	na		na		3.5	Apr†	3.9
Ireland	+ 6.1	Q1	na	na	na	+ 2.7	Apr	+ 2.5	Apr	4.5	May	4.4
Luxembourg	+ 2.1	2003	na	na	na	– 1.2	Dec	+ 0.3	Feb	4.3	Apr	3.6
New Zealand	+ 4.4	Q1	+ 8.1	na	na	+ 3.2	Q4	+ 8.0	Q1	4.3	Q1	4.9
Norway	+ 2.9	Q1	+ 3.9	na	na	+ 5.5	May	+ 1.2	May	4.5	Q1	4.4
Portugal	+ 0.1	Q1	+ 2.4	na	na	– 1.8	May	+ 0.5	May	6.4	Q1†	6.4

*% change on previous quarter at an annual rate. †Not seasonally adjusted. ‡New series. ††Feb-Apr; claimant count rate 2.8% in May. §EU harmonised rate 9.8% in Jun. **Mar-May.

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Prices and wages

Jul 8th 2004
From The Economist print edition

% change on year ago

	Consumer prices		The Economist poll consumer prices forecast		Producer prices		Wages/earnings	
	latest	year ago	2004	2005	latest	year ago	latest	year ago
Australia	+ 2.0 Q1	+ 3.4	+ 2.5	+ 2.6	– 1.1 Q1	+ 3.0	+ 5.1 Q1	+ 4.4
Austria	+ 2.1 May	+ 1.1	+ 1.6	+ 1.5	+ 5.9 Jun	+ 1.7	+ 2.1 May	+ 2.1
Belgium	+ 2.3 Jun	+ 1.6	+ 1.7	+ 1.5	+ 3.9 May	– 0.4	+ 2.3 Apr	+ 1.7
Britain	+ 1.5 May*	+ 1.2	+ 1.5	+ 1.9	+ 2.4 May	+ 1.1	+ 4.3 Apr†	+ 3.2
Canada	+ 2.5 May	+ 2.9	+ 1.9	+ 2.1	+ 5.5 May	– 1.9	+ 3.0 Mar	+ 1.6
Denmark	+ 1.3 May	+ 2.2	+ 1.3	+ 1.9	+ 2.8 May	– 0.6	+ 3.3 Q1	+ 3.9
France	+ 2.6 May	+ 1.8	+ 2.1	+ 1.6	+ 2.3 May	+ 0.7	+ 2.8 Q1	+ 2.9
Germany	+ 1.8 Jun	+ 1.0	+ 1.6	+ 1.2	+ 3.6 May	– 0.4	+ 1.1 Apr	+ 3.3
Italy	+ 2.4 Jun	+ 2.7	+ 2.2	+ 2.1	+ 2.9 May	+ 1.6	+ 3.3 May	+ 1.7
Japan	– 0.5 May	– 0.2	– 0.1	+ 0.2	+ 1.1 May	– 1.1	+ 1.2 May	+ 2.4
Netherlands	+ 1.4 Jun	+ 1.9	+ 1.5	+ 1.4	+ 4.0 May	+ 0.6	+ 1.6 May	+ 3.0
Spain	+ 3.4 May	+ 2.7	+ 2.8	+ 2.6	+ 3.8 May	+ 0.7	+ 3.2 Q1	+ 4.9
Sweden	+ 0.7 May	+ 1.9	+ 0.9	+ 1.6	+ 1.2 May	– 1.4	+ 1.5 Apr	+ 3.1
Switzerland	+ 1.1 Jun	+ 0.6	+ 0.7	+ 1.1	+ 1.4 May	– 0.5	+ 1.4 2003	+ 1.8
United States	+ 3.1 May	+ 2.1	+ 2.5	+ 2.2	+ 4.9 May	+ 2.4	+ 2.0 Jun	+ 2.7
Euro area	+ 2.4 Jun	+ 1.9	+ 2.0	+ 1.7	+ 2.4 May	+ 1.4	+ 2.3 Q1	+ 3.0
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*							
Finland	– 0.1 May	+ 0.7	na	na	+ 1.6 May	– 0.7	+ 4.1 Q1	+ 4.1
Greece	+ 2.9 May	+ 3.8	na	na	+ 3.1 May	+ 2.4	na	na
Iceland	+ 3.9 Jun	+ 1.8	na	na	+ 5.0 May	+ 3.0	+ 4.6 May	+ 5.6
Ireland	+ 1.7 May	+ 3.7	na	na	– 0.1 May	–10.0	+ 6.1 Q4	+ 6.4
Luxembourg	+ 2.3 May	+ 1.9	na	na	+ 2.3 Mar	+ 2.6	– 0.4 Dec	+ 0.7
New Zealand	+ 1.5 Q1	+ 2.5	na	na	– 0.6 Q1	– 1.3	+ 2.2 Q1	+ 2.3
Norway	+ 1.0 May	+ 2.1	na	na	+18.8 May	– 4.5	+ 4.6 Q1	+ 5.3
Portugal	+ 2.4 May	+ 3.7	na	na	+ 1.8 May	+ 1.1	+ 2.6 Mar	– 2.6

*New series. RPI inflation rate in May: 2.8%. †Feb-Apr.

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Economic forecasts

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The Economist poll of forecasters, July averages (previous month's, if changed)

	Real GDP, % change Low/high range		Real GDP, % change average		Consumer prices % increase		Current account % of GDP	
	2004	2005	2004	2005	2004	2005	2004	2005
Australia	2.9/4.0	2.7/3.6	3.5 (3.8)	3.4 (3.1)	2.5 (2.3)	2.6	–5.3(–5.2)	–4.7 (–4.5)
Austria	1.3/2.0	1.7/2.4	1.6	2.1 (1.9)	1.6 (1.5)	1.5	–0.4 (0.4)	–0.5 (0.5)
Belgium	1.7/2.3	1.3/2.6	2.2 (1.9)	2.1 (2.0)	1.7 (1.5)	1.5	3.4 (3.9)	3.5 (3.9)
Britain	2.8/3.6	1.8/3.3	3.2 (3.1)	2.7 (2.6)	1.5	1.9 (1.8)	–2.6	–2.6
Canada	2.5/3.3	2.9/4.2	3.0 (2.8)	3.4 (3.3)	1.9 (1.6)	2.1 (2.0)	2.4 (1.8)	1.8 (1.3)
Denmark	1.2/2.2	1.6/2.6	1.9 (2.0)	2.2	1.3 (1.4)	1.9 (2.0)	2.5 (2.6)	2.4 (2.5)
France	1.5/2.5	1.4/2.7	2.2 (2.1)	2.2	2.1 (2.0)	1.6	0.8 (0.9)	0.8
Germany	1.1/1.8	1.1/2.5	1.4	1.7	1.6 (1.4)	1.2	2.6	2.6
Italy	0.8/1.5	0.9/2.4	1.2 (1.1)	1.8 (1.7)	2.2	2.1	–0.9(–1.0)	–0.8 (–0.9)
Japan	4.0/5.0	1.1/3.7	4.4 (4.1)	2.2 (2.1)	–0.1	0.2 (0.1)	3.4 (3.3)	3.4 (3.3)
Netherlands	0.5/1.9	1.2/2.5	1.3 (1.1)	1.8 (1.7)	1.5 (1.4)	1.4 (1.3)	2.8 (2.6)	2.9 (2.7)
Spain	2.5/3.1	2.5/3.0	2.8	2.8	2.8 (2.6)	2.6	–2.9	–3.1 (–3.0)
Sweden	2.4/3.2	1.9/3.4	2.8 (2.5)	2.5	0.9 (0.8)	1.6	6.3 (5.9)	6.0 (5.6)
Switzerland	1.6/2.0	1.3/2.3	1.9 (1.7)	2.0 (1.9)	0.7 (0.4)	1.1 (0.9)	10.8(10.6)	10.6 (10.3)
United States	4.2/5.0	3.1/4.5	4.6 (4.7)	3.6	2.5 (2.3)	2.2 (2.0)	–5.2(–5.1)	–5.0 (–5.1)
Euro area	1.4/2.0	1.4/2.6	1.8 (1.7)	2.0	2.0 (1.8)	1.7	0.5 (0.4)	0.5 (0.4)

Sources: ABN Amro, Deutsche Bank, Economist Intelligence Unit, Goldman Sachs, HSBC Securities, KBC Bank, J.P. Morgan Chase, Morgan Stanley, Decision Economics, BNP Paribas, Royal Bank of Canada, Citigroup, Scotiabank, UBS

Every month *The Economist* calculates the average of a group of forecasters' predictions for economic growth, inflation and current-account balances for 15 countries and for the euro area. The table also shows the highest and lowest projections for growth. The previous month's figures, where they are different, are shown in brackets. The panel has again raised its forecast for GDP growth in Japan in 2004, from 4.1% in June to 4.4%. It has nudged up this year's projection for growth in the euro area to 1.8%, but has nudged down the forecast for America to 4.6%. It now expects Britain to grow a bit faster, by 3.2% this year and by 2.7% in 2005. The panel has again become more worried about inflation in America, raising its forecasts to 2.5% in 2004 and 2.2% in 2005. It also expects higher inflation in the euro area, where consumer prices are now forecast to rise by 2.0% in 2004.

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Money and interest rates

Jul 8th 2004
From The Economist print edition

	Money supply* % change on year ago			Interest rates % p.a. (Jul 7th 2004)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+ 4.3	+10.3	May	5.48	4.73	5.24	5.80	5.11	6.58
Britain	+ 5.3	+ 7.8	May	4.78	3.53	4.80	5.02	4.29	5.82
Canada	+12.4	+ 8.6	May	2.00	3.10	3.08	4.82	4.71	6.36
Denmark	+ 7.9	+ 9.0	May	2.25	2.25	2.50	4.34	4.07	5.54
Japan	+ 3.6	+ 1.8	Jun	0.02	0.01	0.15	1.77	1.09	1.88
Sweden	+ 0.7	+ 3.7	May	1.98	2.69	2.85	4.51	4.25	2.95
Switzerland	+ 9.4	+ 4.3	May	0.48	0.27	1.28	2.84	2.33	2.60
United States	+ 5.1	+ 5.5	May	1.49	1.08	2.53	4.47	3.70	5.96
Euro area†	+ 9.3	+ 4.7	May	2.11	2.13	2.52	4.19	3.87	4.04

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. Benchmarks: US 30-year 5.23%, Japan No. 261 1.79%. Central bank rates: US fed funds 1.25%, ECB refinancing 2.00%, BOJ overnight call 0.001%, BOE repo 4.5%. Sources: Commerzbank, Danske Bank, J.P. Morgan Chase, Royal Bank of Canada, Stockholmsbörsen, UBS, Global Insight, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

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The Economist commodity price index

Jul 8th 2004
From The Economist print edition

1995=100

	Jun 29th	Jul 6th*	% change on one month	% change on one year
Dollar index				
All items	94.7	96.4	+ 1.4	+26.2
Food	92.1	94.0	+ 1.1	+23.1
Industrials				
All	98.3	99.7	+ 1.6	+30.4
Nfa†	92.4	92.1	– 2.3	+15.5
Metals	103.3	106.1	+ 4.7	+44.0
Sterling index				
All items	82.6	82.7	+ 1.1	+12.2
Euro index				
All items	102.8	103.3	+ 1.3	+16.2
Yen index				
All items	109.2	112.1	+ 0.9	+16.5
Gold				
$ per oz	394.00	391.15	– 0.3	+13.6
West Texas Intermediate				
$ per barrel	35.61	39.65	+ 6.7	+31.1

* Provisional. † Non-food agriculturals.

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Stockmarkets

Jul 8th 2004
From The Economist print edition

Market indices

	Jul 7th	2004 high	2004 low	% change on one week	% change on record high	% change on Dec 31st 2003 in local currency	% change on Dec 31st 2003 in $ terms
Australia (All Ordinaries)	3,559.9	3,559.9	3,274.9	+ 0.8	nil	+ 7.7	+ 3.2
Austria (ATX)	1,998.1	2,015.3	1,568.9	+ 0.4	- 0.9	+29.3	+26.7
Belgium (Bel 20)	2,451.8	2,517.3	2,244.2	- 0.8	-33.4	+ 9.2	+ 7.1
Britain (FTSE 100)	4,358.4	4,575.7	4,309.4	- 2.4	-37.1	- 2.6	+ 0.8
Canada (Toronto Composite)	8,481.9	8,898.8	8,123.5	- 0.7	-25.5	+ 3.2	+ 0.8
Denmark (KBX)	239.9	241.3	219.0	+ 0.5	-20.5	+12.3	+10.3
France (SBF 250)	2,504.1	2,594.4	2,411.5	- 1.8	-43.0	+ 3.8	+ 1.8
(CAC 40)	3,660.4	3,811.4	3,465.3	- 1.9	-47.1	+ 2.9	+ 0.8
Germany (DAX)	3,930.6	4,151.8	3,726.1	- 3.0	-51.3	- 0.9	- 2.8
Italy (BCI)	1,311.4	1,340.3	1,239.5	- 1.2	-39.9	+ 4.4	+ 2.3
Japan (Nikkei 225)	11,384.9	12,163.9	10,365.4	- 4.0	-70.7	+ 6.6	+ 5.4
(Topix)	1,139.9	1,217.9	1,022.6	- 4.2	-60.5	+ 9.2	+ 7.9
Netherlands (AEX)	334.8	364.8	323.0	- 3.0	-52.3	- 0.8	- 2.8
Spain (Madrid SE)	850.2	881.7	808.0	nil	-25.8	+ 5.2	+ 3.1
Sweden (Affarsvarlden Gen)	202.4	218.1	188.5	- 1.7	-49.4	+ 7.4	+ 4.2
Switzerland (Swiss Market)	5,541.4	5,934.4	5,469.0	- 1.4	-34.1	+ 1.0	+ 1.7
United States (DJIA)	10,240.3	10,737.7	9,906.9	- 1.9	-12.6	- 2.0	- 2.0
(S&P 500)	1,118.3	1,157.8	1,084.1	- 2.0	-26.8	+ 0.6	+ 0.6
(NASDAQ Comp)	1,966.1	2,153.8	1,876.6	- 4.0	-61.1	- 1.9	- 1.9
Europe (FTSE Eurotop 300)*	981.7	1,026.2	957.9	- 1.7	-42.4	+ 2.5	+ 0.4
Euro area (FTSE Ebloc 100)*	837.0	888.3	806.7	- 1.9	-46.0	+ 0.6	- 1.4
World (MSCI)†	1,048.5	1,085.8	997.0	- 1.3	-27.6	+ 1.2	+ 1.2
World bond market (Citigroup)‡	603.1	619.5	575.1	+ 1.4	- 2.7	- 0.1	- 0.1

*In euro terms. †Morgan Stanley Capital International index includes individual markets listed above plus eight others, in $ terms.
‡Citigroup World Government Bond Index, total return, in $ terms.

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Trade, exchange rates and budgets

Jul 8th 2004
From The Economist print edition

	Trade balance*, $bn latest 12 months		Current account $bn latest 12 mths		The Economist poll % of GDP, forecast 2004	2005	Exchange rate trade-weighted† 1990=100 Jul 7th	year ago	Currency units per $ Jul 7th	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2004‡
Australia	− 16.6	May	− 33.0	Q1	− 5.3	− 4.7	84.6	82.1	1.38	1.53	2.57	1.71	1.28	0.5
Austria	− 0.8	Mar	− 1.4	Apr	− 0.4	− 0.5	102.8§	102.3	0.81	0.88	1.50	–	0.75	-1.3
Belgium	+ 21.8	Apr	+ 12.2	Mar	+ 3.4	+ 3.5	102.7§	102.2	0.81	0.88	1.50	–	0.75	-0.2
Britain	− 89.4	Apr	− 39.2	Q1	− 2.6	− 2.6	105.8	100.0	0.54	0.61	–	0.67	0.50	-2.9
Canada	+ 47.8	Apr	+ 20.9	Q1	+ 2.4	+ 1.8	87.0	86.0	1.32	1.38	2.45	1.63	1.22	1.2
Denmark	+ 9.2	Apr	+ 6.4	Apr	+ 2.5	+ 2.4	106.5	106.2	6.01	6.57	11.2	7.43	5.55	0.9
France	+ 4.6	Apr	+ 10.5	Apr	+ 0.8	+ 0.8	106.1§	105.4	0.81	0.88	1.50	–	0.75	-3.8
Germany	+174.2	Apr	+ 74.3	Apr	+ 2.6	+ 2.6	103.8§	102.9	0.81	0.88	1.50	–	0.75	-3.7
Italy	+ 2.6	Apr	− 16.2	Apr	− 0.9	− 0.8	75.7§	75.1	0.81	0.88	1.50	–	0.75	-3.1
Japan	+121.4	Apr	+157.2	Apr	+ 3.4	+ 3.4	134.9	129.7	108	118	201	134	–	-7.1
Netherlands	+ 33.1	Apr	+ 18.7	Q1	+ 2.8	+ 2.9	102.1§	101.6	0.81	0.88	1.50	–	0.75	-3.1
Spain	− 58.7	Apr	− 27.0	Mar	− 2.9	− 3.1	76.9§	76.6	0.81	0.88	1.50	–	0.75	0.3
Sweden	+ 21.7	May	+ 21.2	Q1	+ 6.3	+ 6.0	81.0	80.6	7.42	8.08	13.8	9.17	6.84	0.2
Switzerland	+ 7.9	May	+ 37.5	Q1	+10.8	+10.6	114.3	111.6	1.23	1.37	2.28	1.52	1.13	-1.6
United States	−568.9	Apr	−537.3	Q1	− 5.2	− 5.0	95.8	103.6	–	–	1.86	1.24	0.92	-4.7
Euro area	+103.0	Apr	+ 52.8	Apr	+ 0.5	+ 0.5	90.5	89.6	0.81	0.88	1.50	–	0.75	-2.8
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 14.8	Apr	+ 11.2	Apr	na	na	81.7§	81.1	0.83	0.88	1.54	–	0.77	1.6
Greece	− 27.2	Apr	− 10.4	Apr	na	na	59.4§	59.1	0.83	0.88	1.54	–	0.77	-3.2
Iceland	− 0.3	May	− 0.7	Q1	na	na	96.5**	97.2	72.7	77.6	135	89.9	67.0	0.2
Ireland	+ 42.7	Apr	− 2.1	Q1	na	na	93.6§	93.4	0.83	0.88	1.54	–	0.77	-0.5
Luxembourg	− 3.9	Apr	+ 3.2	Q1	na	na	102.7§	102.2	0.83	0.88	1.54	–	0.77	-1.8
New Zealand	− 2.1	May	− 3.4	Q1	na	na	103.7	99.4	1.60	1.71	2.97	1.98	1.48	2.9
Norway	+ 28.6	May	+ 28.9	Apr	na	na	95.3	96.6	6.93	7.33	12.9	8.57	6.39	10.4
Portugal	− 14.4	Mar	− 8.3	Apr	na	na	93.6**	92.7	0.83	0.88	1.54	–	0.77	-3.8

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †Bank of England except §IMF, April average. ‡OECD forecast. **IMF, March average.

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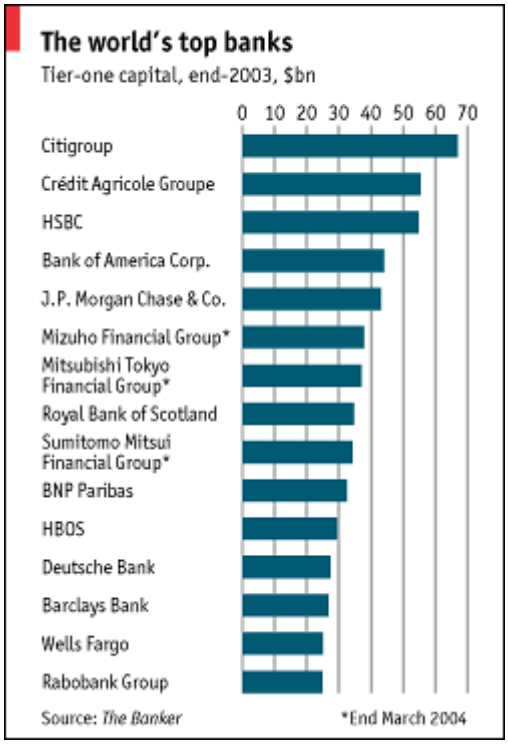
The world's top banks

Jul 8th 2004
From The Economist print edition



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Overview

Jul 8th 2004
From The Economist print edition

Taiwan ran a trade deficit in June, causing the 12-month surplus to fall to $13.1 billion. **South Korea's** trade surplus increased to $27.5 billion over the same period.

In **Malaysia**, industrial production rose by 12.8% in the year to May. In **South Africa**, manufacturing output increased by 3.0% over the same period.

In the **Philippines**, the 12-month inflation rate rose from 4.5% to 5.1% in June, the highest rate for more than two years. In **Turkey**, it stayed put in June at 8.9%; a year ago, inflation was 29.8%.

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Poland

Jul 8th 2004
From The Economist print edition

The OECD believes that Poland will grow by around 4.5% a year in 2004 and 2005. The recovery is being boosted by rising exports and higher investment. But the unemployment rate is over 19% and only one in two Poles of working age has a job. The OECD says that the government should help people to move out of struggling rural areas. It also recommends measures to make the labour market function better, including the reform of disability benefits.

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Economy

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	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 9.8	Q1	+17.5	May	+ 4.4	May	+15.6	May	+45.9	2003	444.4	Mar
Hong Kong	+ 6.8	Q1	+ 1.8	Q1	– 0.9	May	–12.3	May	+14.3	Q1	120.8	Jun
India	+ 8.2	Q1	+ 9.4	Apr	+ 2.8	May	–16.4	May	+ 8.7	Q1	114.1	Jun
Indonesia	+ 4.5	Q1	+17.1	Apr	+ 6.8	Jun	+27.8	May	+ 7.4	Q4	35.3	May
Malaysia	+ 7.6	Q1	+12.8	May	+ 1.2	May	+20.1	May	+13.0	Q1	53.6	May
Philippines	+ 6.4	Q1	– 5.2	Apr	+ 5.1	Jun	– 1.7	Apr	+ 3.9	Mar	13.0	Jun
Singapore	+ 7.5	Q1	+21.0	May	+ 2.0	May	+15.1	May	+27.6	Q1	101.6	Jun
South Korea	+ 5.3	Q1	+13.5	May	+ 3.6	Jun	+27.5	Jun	+24.1	May	166.5	May
Taiwan	+ 6.3	Q1	+16.6	May	+ 1.8	Jun	+13.1	Jun	+27.4	Q1	230.1	Jun
Thailand	+ 6.5	Q1	+ 6.8	May	+ 3.0	Jun	+ 2.2	May	+ 7.4	May	41.8	May
Argentina	+10.7	Q1	+ 6.2	May	+ 4.9	Jun	+14.2	May	+ 6.1	Q1	16.7	May
Brazil	+ 2.7	Q1	+ 6.7	Apr	+ 5.2	May	+29.5	Jun	+ 6.5	May	50.5	May
Chile	+ 4.8	Q1	+ 4.5	May	+ 1.1	Jun	+ 6.2	Jun	– 0.1	Q1	61.1	May
Colombia	+ 3.8	Q1	+ 3.8	Apr	+ 6.1	Jun	+ 0.2	Apr	– 1.6	Q1	11.3	Apr
Mexico	+ 3.7	Q1	+ 4.0	Apr	+ 4.3	May	– 5.4	May	– 9.1	Q1	60.3	May
Peru	+ 3.3	Apr	+ 5.6	Apr	+ 4.3	Jun	+ 1.4	Apr	– 0.6	Q1	10.4	May
Venezuela	+29.8	Q1	+24.6	Apr	+22.3	Jun	+17.8	Q1	+12.3	Q1	17.8	Mar
Egypt	+ 3.1	2003†	+ 2.6	2003†	+ 5.5	Dec	– 6.7	Q1	+ 3.9	Q1	13.6	Feb
Israel	+ 2.6	Q1	– 0.5	Apr	– 0.6	May	– 5.9	May	+ 0.3	Q1	26.1	Jun
South Africa	+ 1.9	Q1	+ 3.0	May	+ 0.6	May	+ 1.1	May	– 2.0	Q1	9.8	Jun
Turkey	+10.1	Q1	+16.5	May	+ 8.9	Jun	–26.8	Apr	– 9.8	Apr	33.2	May
Czech Republic	+ 3.1	Q1	+10.1	Apr	+ 2.7	May	– 2.5	May	– 6.0	Q1	26.4	May
Hungary	+ 4.2	Q1	+ 7.1	May	+ 7.6	May	– 4.2	Apr	– 7.1	Apr	13.1	May
Poland	+ 6.9	Q1	+12.3	May	+ 3.4	May	– 6.0	Apr	– 3.1	Apr	35.3	May
Russia	+ 7.4	Q1	+ 5.5	May	+10.2	Jun	+65.7	Apr	+35.3	Q1	81.5	Jun
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Estonia	+ 6.8	Q1	+ 7.9	May	+ 3.7	May	– 2.2	Apr	– 1.1	Q1	1.3	Apr
Latvia	+ 8.8	Q1	+ 9.4	Apr	+ 6.2	May	– 2.3	Apr	– 1.3	Apr	1.7	Apr
Lithuania	+ 7.7	Q1	na		+ 1.1	May	– 2.9	Apr	– 1.5	Q1	3.3	Apr
Slovakia	+ 5.5	Q1	+ 5.7	May	+ 8.3	May	– 0.4	Apr	nil	Mar	11.6	Apr
Slovenia	+ 3.7	Q1	– 0.9	Apr	+ 3.9	Jun	– 0.9	Apr‡	– 0.1	Apr	8.3	Mar
Pakistan	+ 5.1	2003†	+13.4	Feb	+ 7.1	May	– 3.2	Jun	+ 2.4	Q1	11.1	May
Saudi Arabia	+ 7.2	2003	na		+ 0.6	Apr	+61.2	2003	+29.7	2003	23.2	May

*Excluding gold, except Singapore; IMF definition. †Year ending June.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Akbank; Deutsche Bank

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Financial markets

Jul 8th 2004
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Jul 7th		Dec 31st 2003	
	Jul 7th	year ago	Jul 7th	% p.a.		one week	in local currency	in $ terms
China	8.28	8.28	15.3	3.20	1,509.9	+2.8	– 3.8	– 3.8
Hong Kong	7.80	7.80	14.5	0.49	12,320.3	+0.3	– 2.0	– 2.5
India	45.8	46.2	84.9	4.49	4,956.0	+3.3	– 15.1	– 15.4
Indonesia	9,000	8,196	16,689	7.57	771.7	+5.4	+ 11.5	+ 4.4
Malaysia	3.80	3.80	7.05	2.87	855.1	+4.3	+ 7.7	+ 7.7
Philippines	55.9	53.4	103.7	8.00	1,598.4	+1.2	+ 10.8	+ 10.0
Singapore	1.71	1.75	3.17	0.88	1,873.8	+1.9	+ 6.2	+ 5.6
South Korea	1,152	1,179	2,135	3.91	761.9	–3.0	– 6.0	– 2.8
Taiwan	33.5	34.3	62.2	1.10	5,727.8	–1.9	– 2.8	– 1.6
Thailand	40.8	41.7	75.6	1.34	666.4	+3.1	– 13.7	– 16.2
Argentina	2.95	2.77	5.46	5.38	970.0	+2.6	– 9.5	– 10.0
Brazil	3.03	2.87	5.62	15.81	21,172.8	+0.1	– 4.8	– 9.4
Chile	631	704	1,170	1.80	7,612.4	+1.2	+ 3.8	– 2.6
Colombia	2,681	2,849	4,970	7.81	2,973.1	–1.0	+ 27.4	+ 32.1
Mexico	11.5	10.5	21.3	6.69	10,042.0	–2.3	+ 14.2	+ 11.7
Peru	3.46	3.47	6.42	2.36	2,896.4	+0.4	+ 18.9	+ 19.0
Venezuela	2,558§	1,598	4,744	12.32	24,843.6	–1.7	+ 11.9	+ 24.7
Egypt	6.20	6.06	11.50	11.03	14,648.1	+1.6	+ 25.9	+ 25.1
Israel	4.48	4.32	8.31	1.00	597.2	+0.2	+ 11.8	+ 9.6
South Africa	6.11	7.60	11.3	8.20	10,037.7	–0.7	– 3.4	+ 5.7
Turkey	1,440,500	1,420,500	2,671,119	25.10	18,296.7	+1.8	– 1.8	– 4.2
Czech Republic	25.4	27.9	47.2	2.46	789.9	–0.5	+ 19.8	+ 21.0
Hungary	202	232	375	11.43	11,756.3	+1.9	+ 25.3	+ 28.6
Poland	3.66	3.93	6.78	6.26	23,766.6	–0.8	+ 14.2	+ 16.9
Russia	29.1	30.4	53.9	13.00	572.3‡	–1.9	+ 0.3	+ 0.9
EMF (MSCI)*	1.00	1.00	1.85	na	431.9	–0.1	– 2.5	– 2.5
EMBI+†	1.00	1.00	1.85	na	290.4	+1.3	– 1.5	– 1.5

*Emerging Mkts Free. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡In $ terms. §Floating exchange rate.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Akbank; Deutsche Bank

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